Report of the
AUDITOR GENERAL
to the
Legislative Assembly

2009

Prince Edward Island

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Prince Edward Island | Ile-du-Prince-Édouard

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The Honourable Speaker and
Members of the Legislative Assembly
of the Province of Prince Edward Island

In accordance with the requirements of the Audit Act, I have the honour of presenting my Annual Report to the Legislative Assembly.

Respectfully submitted,

Colin Younker, CA
Auditor General

Charlottetown
Prince Edward Island
March 10, 2009

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INTRODUCTION

REPORT OVERVIEW

Under the Audit Act, the Auditor General is required to report annually to the Legislative Assembly. My 2009 Annual Report provides observations, recommendations, and information pertaining to the audits and examinations of government operations conducted by the Office during the year. The purpose of this report is to assist the Legislative Assembly in carrying out its responsibility to hold government accountable for the management of public resources.

My 2009 Annual Report deals mainly with matters pertaining to the 2007-08 fiscal year, however, many of the issues identified remain current and are still being addressed by government.

It is not possible to audit all government programs and entities each year, however, with the resources available the Office strives to provide reasonable audit coverage on a cyclical basis. A large portion of the audit work is determined by statutory requirements which name the Auditor General as auditor. These requirements include the annual audit of the Public Accounts of the Province. The remainder of our resources are devoted to special audits and examinations.

This report includes information and discussion on the **Province's Finances**. The section on **Special Audits and Examinations** includes the results of various examinations conducted during the year. Pursuant to Section 14(d) of the Audit Act, our Office was requested by the Lieutenant Governor in Council to carry out a special investigation into the financial relationship and transactions between the Province, Natural Organic Food Group PEI Inc. and the related company, Natural Organic Food Group Inc. (Quebec). Our report was provided to Executive Council in November 2008, and it is included in this Annual Report. In addition, this Annual Report summarizes the results of the following audits: Provincial Nominee Program-Immigrant Partner Category, In-Province Physician Payments, and Department of Social Services and Seniors - Grants to Non-Government Organizations. The **Financial Statement Audits** section provides information on significant issues arising from the financial statement audits and other audit procedures conducted by the Office.

As part of our work, we provide recommendations to departments and agencies to improve the management and administration of government operations and programs. On an annual basis, we contact departments and agencies to obtain follow-up information on the status of any outstanding recommendations from previous years. This information is included in a separate section of the report entitled **Update on Previous Recommendations.**

The **Standing Committee on Public Accounts** reviews the Auditor General's Annual Report and plays an important role in holding government accountable for the management of public resources. Information on the role of this Committee, and its proceedings during the past year, is provided in a separate section of the report.

The section on the **Office of the Auditor General** provides information on the mission and mandate of the Office as well as the responsibilities of the Auditor General. Background information is provided on the objectives and accomplishments of the Office and the resources used to achieve them.

ACKNOWLEDGEMENTS

Cooperation of Ministers, Deputy Ministers, heads of Crown agencies and their staff is important. To carry out our work, it is imperative that we receive the necessary information, reports and explanations. I wish to acknowledge that my Office received cooperation in the completion of the audits covered in my Annual Report.

The preparation of this report as well as the statutory audits conducted by the Office is the result of the support and dedication of my staff. I would like to thank them for the professional manner in which they conduct themselves and perform their work. The continued success of the Office is dependent upon their effort and commitment.

INTRODUCTION

APERÇU DU RAPPORT

En vertu de la *Audit Act* (loi sur la vérification des comptes publics), le vérificateur général doit faire rapport chaque année à l'Assemblée législative. Mon rapport annuel 2009 fournit des observations, des recommandations et des renseignements sur les vérifications et les examens des activités de gouvernement menés par le Bureau au cours de l'année. Le but de ce rapport est d'aider l'Assemblée législative à s'acquitter de sa responsabilité de tenir le gouvernement responsable de la gestion des ressources publiques.

Mon rapport annuel 2009 traite principalement d'affaires portant sur l'exercice financier 2007-08; toutefois, plusieurs des points mis en évidence demeurent actuels et font toujours partie des préoccupations du gouvernement.

Il n'est pas possible de vérifier tous les programmes et entités du gouvernement chaque année; toutefois, avec les ressources à sa disposition, le Bureau s'efforce d'assurer une couverture de vérification raisonnable sur une base cyclique. Une bonne partie du travail de vérification est définie par les exigences statutaires qui nomment le vérificateur général à titre de vérificateur. Ces exigences comprennent la vérification annuelle des comptes publics de la province. Le reste de nos ressources sont consacrées à des vérifications et à des examens spéciaux.

Le présent rapport comprend des renseignements et une discussion sur les **finances de la province**. La section sur les **vérifications et examens spéciaux** comprend les résultats de divers examens menés durant l'année. Conformément à l'article 14(d) de la *Audit Act*, le lieutenant-gouverneur a demandé à notre Bureau de procéder à une enquête spéciale portant sur les transactions et les rapports financiers entre la province, Natural Organic Food Group PEI Inc. et la compagnie liée, Natural Organic Food Group Inc. (Québec). Nous avons remis notre rapport au Conseil exécutif en novembre 2008, et il est inclus dans le présent rapport. De plus, ce rapport résume les résultats des vérifications suivantes : la Catégorie des immigrants partenaires dans le cadre du Programme des candidats de la province de l'Île-du-Prince-Édouard, les Paiements aux médecins de

la province, et Subventions aux organismes non gouvernementaux du ministère des Services sociaux et des Aînés. La section de la **vérification des états financiers** fournit des renseignements sur les questions importantes découlant des vérifications des états financiers et d'autres procédures de vérification menées par le Bureau. Dans le cadre de notre travail, nous offrons des recommandations aux ministères et organismes afin d'améliorer la gestion et l'administration des activités et des programmes du gouvernement. Sur une base annuelle, nous communiquons avec les ministères afin d'obtenir des compléments d'information sur le statut de l'une ou l'autre des recommandations des années précédentes. Ces renseignements sont compris dans une section séparée du rapport intitulée *Update on Previous Recommendations* (mise à jour des recommandations antérieures).

Le **Comité permanent sur les comptes publics** révise le rapport annuel du vérificateur général et joue un rôle important en rendant le gouvernement responsable de la gestion des ressources publiques. Les renseignements sur le rôle de ce Comité, et de ses travaux au cours de la dernière année, apparaissent dans une section particulière du rapport.

La section sur le **Bureau du vérificateur général** offre des renseignements sur la mission et le mandat du Bureau, ainsi que les responsabilités du vérificateur général. Des renseignements généraux sont fournis sur l'objectif et les réalisations du Bureau ainsi que les ressources utilisées pour y parvenir.

REMERCIEMENTS

La collaboration des ministres, sous-ministres, chefs d'agence des sociétés d'État et leur personnel est importante. Pour accomplir notre travail, il est impératif que nous recevions les renseignements, rapports et explications nécessaires. J'aimerais indiquer que les vérifications apparaissant dans mon rapport annuel ne se sont pas faites sans collaboration.

La préparation du présent rapport ainsi que les vérifications statutaires menées par le Bureau sont le résultat du soutien et du

dévouement de mon personnel. J'aimerais les remercier pour le professionnalisme dont ils ont fait preuve dans l'exécution de leurs tâches. La réussite soutenue du Bureau tient à leur effort et à leur dévouement.

1. THE PROVINCE'S FINANCES

OVERALL COMMENTS

1.1 Each year we comment on the Province's finances. The financial position of the Province for the most recent fiscal year is discussed and comparisons are made with prior years. This information is important because it indicates where we are financially. The Consolidated Financial Statements are the primary source of information to assess the financial condition of the Province.

1.2 For 2007-08, the Province recorded a deficit of $3.6 million which is a significant decrease from the $23.9 million surplus in 2006-07.

1.3 The net debt increased by $34.9 million or 2.7 percent and stands at $1.35 billion at March 31, 2008. The GDP of the Province grew by 4.8 percent. However, the Province's net debt is still significant.

BACKGROUND

1.4 The Public Accounts record the Government's financial activities in accordance with the recommendations of the Canadian Institute of Chartered Accountants. The statements combine the financial activities of many diverse government programs and entities with expenses of approximately $1.3 billion.

1.5 As in previous years, we are providing information to help put the numbers into perspective. The presentation is made in a format that focuses on key information to assist the Legislature and the public in obtaining a better understanding of the Province's financial condition. The Province's finances have a significant impact on the Provincial economy.

1.6 This discussion of the Province's finances is based on the Consolidated Financial Statements, which include departments, Crown corporations, school boards, and other organizations which are part of the overall government reporting entity.

FINANCIAL MEASURES

1.7 Some of the common terms used to describe the Province's financial condition are presented below.

1.8 The **annual surplus or deficit** is the difference between a government's revenue and expense. This measure shows the extent to which revenues raised in the year were sufficient to cover expenses in that year. For the year ended March 31, 2008 the Province had a deficit of $3.6 million.

1.9 The **total debt** is the amount owed by government. Government's debt includes outstanding debentures, pension obligations, and other accounts payable. The total debt of the Province as of March 31, 2008 was $2 billion.

1.10 **Financial assets** are cash and other assets which could provide resources to pay liabilities or finance future operations. Total financial assets at March 31, 2008 were $732 million.

1.11 The **net debt** is equal to the difference between the government's total liabilities and its financial assets. The net debt of the Province as of March 31, 2008 was $1.35 billion.

1.12 **Non-financial assets** include tangible capital assets such as buildings, roads, and equipment as well as prepaid expenses and inventories. The book value of tangible capital assets increases as they are acquired and is reduced over a period of time through amortization. At March 31, 2008 non-financial assets had a net book value of $587.1 million.

1.13 The **accumulated deficit** represents the Province's liabilities net of the assets the Province has acquired, both financial and non-financial. It is calculated based on the surpluses and deficits incurred over the years. The accumulated deficit at March 31, 2008 was $760 million.

1.14 The **interest charged on borrowings** is the amount required to service the debt and must be taken from revenues before any expenditures can be made on government programs.

1.15 The **gross domestic product (GDP)** is a measure of the value of the goods and services produced in the Province in a year. The Province's GDP is measured and reported by Statistics Canada.

1.16 **Exhibit 1.1** shows a summary of some key financial measures for the Province over the past five years.

EXHIBIT 1.1
PROVINCE OF PRINCE EDWARD ISLAND
SUMMARY OF FINANCIAL INFORMATION
(Millions)

	2008	2007	2006	2005	2004
Surplus (Deficit)	$ (3.6)	$ 23.9	$ .7	$ (33.6)	$ (125.1)
Increase (decrease) in Net Debt	$ 34.9	$ (10.7)	$ (6.6)	$ 16.9	$ 134.1
Net Debt	$1,347.1	$1,312.2	$1,322.9	$1,329.5	$1,312.6
Non-Financial Assets	587.1	560.8	547.6	552.9	582.7
Accumulated Deficit	$ 760.0	$ 751.4	$ 775.3	$ 776.6	$ 729.9
Debt Charges	$ 118.9	$ 120.3	$ 116.8	$ 104.9	$ 106.5
GDP	$ 4,538	$ 4,332	$ 4,142	$ 4,023	$ 3,858

Financial Highlights

1.17 **Exhibit 1.2** shows the change in the surplus from 2006-07 to the deficit in 2007-08.

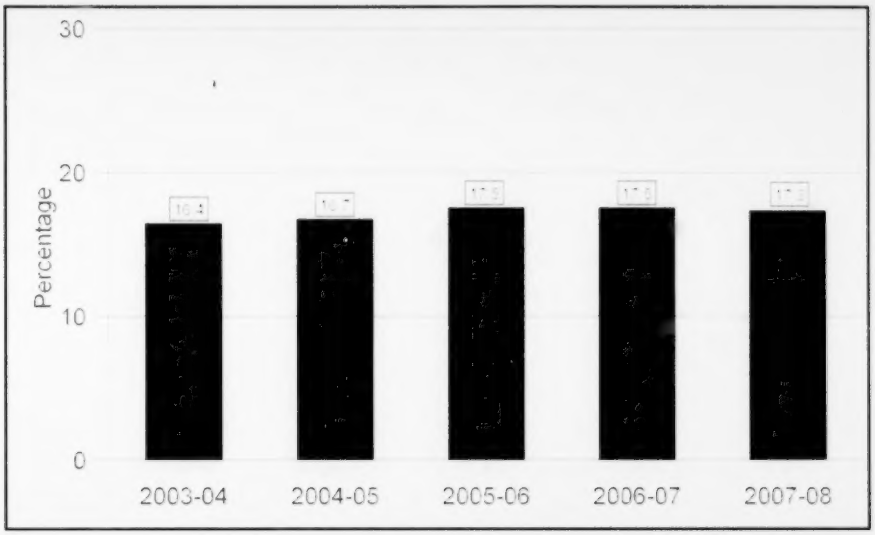
EXHIBIT 1.2
PROVINCE OF PRINCE EDWARD ISLAND
CHANGE IN SURPLUS (DEFICIT)
(Millions)

	Revenue	Expense	Surplus
2006/07 Surplus	$1,232.0	$1,208.1	$23.9
Increased Federal Transfers	43.5	-	-
Increased Tax Revenue	13.4	-	-
Increased Government Business Entities	5.9	-	-
Increased other Government Revenue	7.6	-	-
Increased Health Expense	-	24.5	-
Increased Education Expense	-	23.4	-
Increased Provincial Treasury	-	12.3	-
Increased Communities, Cultural Affairs & Labor	-	11.5	-
Increased Transportation & Public Works	-	9.4	-
Increased Environment Energy & Forestry	-	6.3	-
Increased Social Services & Seniors	-	4.1	-
Increased Other Expense	-	6.4	-
2007/08 (Deficit)	$1,302.4	$1,306.0	$(3.6)

1.18 The growth in revenue for 2007-08 resulted from an increase in both provincial and federal revenue. Provincial tax revenue increased by $13.4 million. Federal revenue increased by $43.5 million. Equalization, which comprises 56.8 percent of federal revenue recorded, increased by $2.7 million while health and social transfers which comprise 26.6 percent of federal revenue increased by $4.7 million. Base funding for infrastructure of $25 million and Canada Eco Trust funding of $5 million provided new federal revenue.

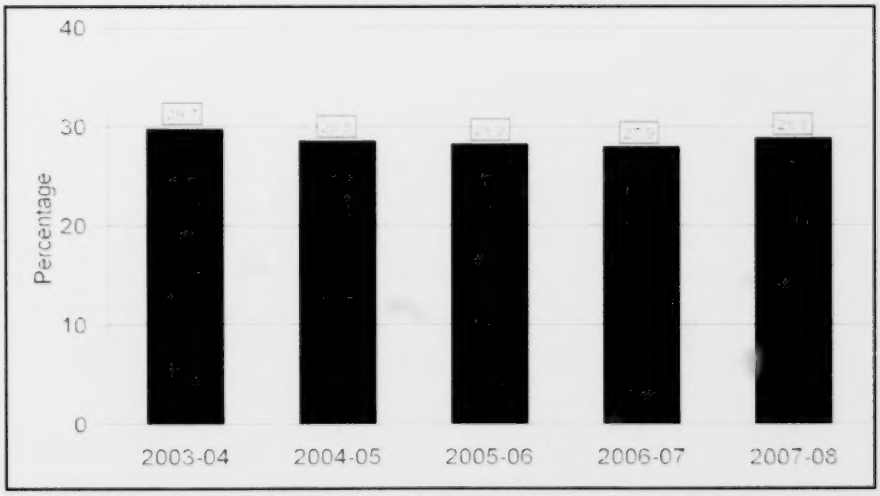
1.19 **Exhibit 1.3** shows the ratio of provincial revenue to GDP for five years ended 2007-08. The ratio has remained relatively stable for the five years ended 2007-08 indicating that government has not been increasing its own source revenue at a rate greater than the growth in the Province's economy.

EXHIBIT 1.3
PROVINCIAL REVENUE AS A PERCENT OF GDP



1.20 Exhibit 1.4 shows that government spending as a percentage of GDP decreased slightly in 2004-05 and remained relatively constant for the next two years and then increased slightly in 2007-08. This indicates that the growth in the economy was sufficient to maintain additional spending.

EXHIBIT 1.4
EXPENSES AS A PERCENT OF GDP

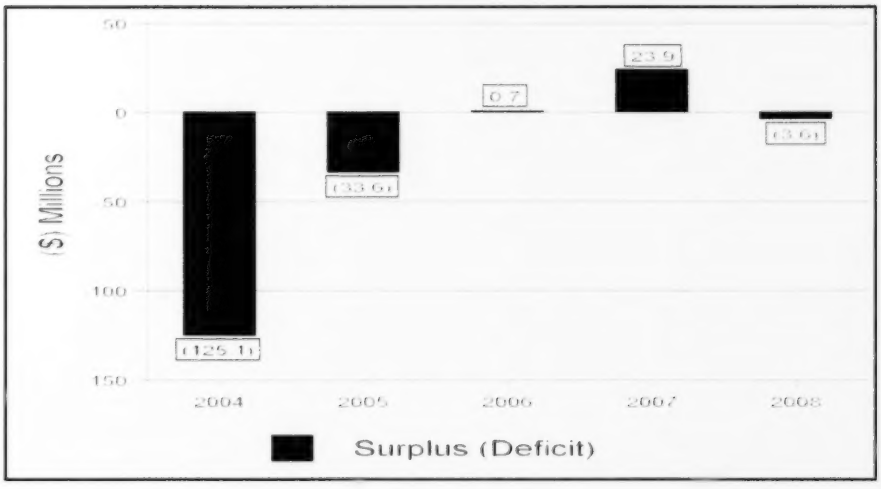


Sustainability

1.21 Sustainability indicates whether the Province can maintain programs and meet existing creditor requirements without increasing the debt burden on the economy. A comparison of the Government's annual surplus or deficit, net debt and the Provincial GDP provides insight into the sustainability of a government's practices of incurring expenditures and generating revenues.

1.22 The annual deficit or surplus indicates the extent to which a government spends more or less than what is raised in revenue in a particular year. It basically shows whether a government is living within its means. **Exhibit 1.5** shows the annual surplus (deficit) for the last five years. For these years the combined total is a deficit of $137.7 million. For 2007-08 the Province recorded a deficit.

EXHIBIT 1.5
THE GOVERNMENT'S SURPLUS (DEFICIT)
2004-2008

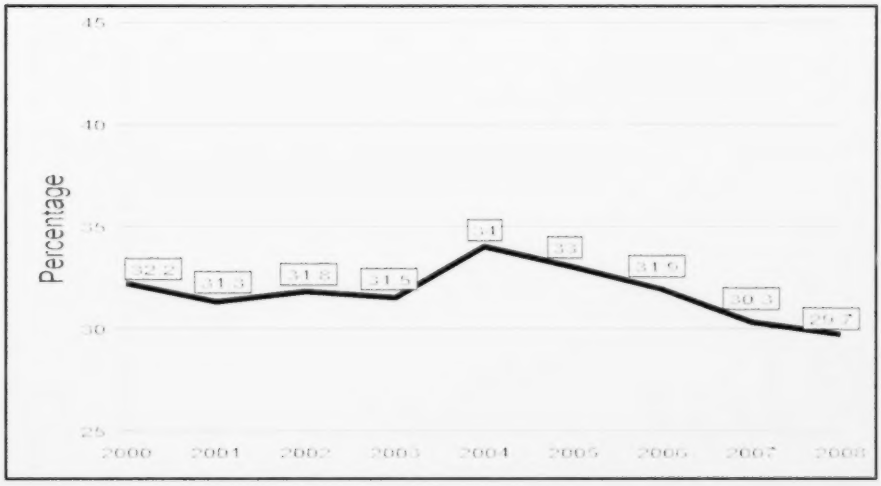


1.23 The net debt is the difference between government's total liabilities and its financial assets. Since 2004 the net debt has increased by $34.5 million totalling $1.35 billion at March 31, 2008.

1.24 The GDP of the Province indicates the size of our economy. The Province's economy supports government operations through taxes and fees. While the net debt has increased by 2.6 percent since 2004, the GDP of the Province increased by 17.6 percent. This is a continuation of the trend from the 2006-07 year and the Province has increased capacity to maintain programs and services without increasing the debt burden in relation to the GDP.

1.25 **Exhibit 1.6** shows the net debt to GDP ratios since 2000. The 2003-04 deficit of $125.1 million caused the net debt to GDP ratio to increase significantly but with the lower deficit of $33.6 in 2005, the surpluses in 2006 and 2007, and the small deficit of $3.6 in 2008, the rates have fallen below the 2000 level.

EXHIBIT 1.6
NET DEBT AS A PERCENT OF GDP



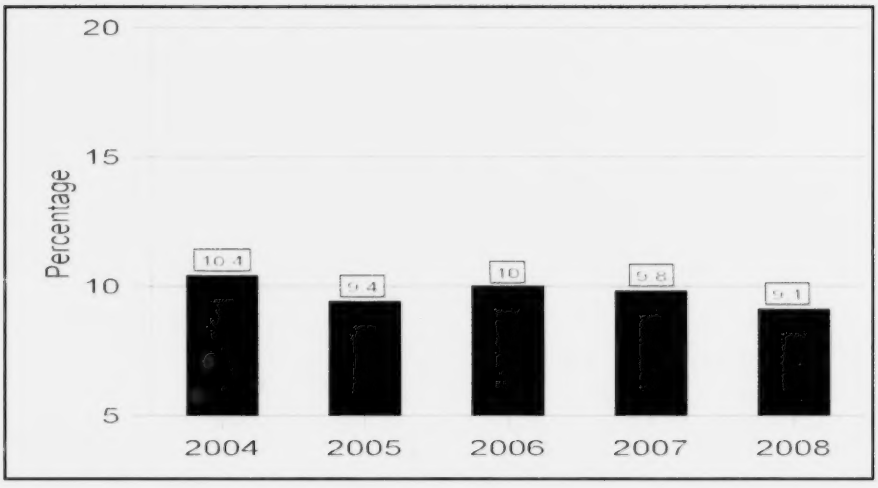
Flexibility

1.26 Government's flexibility is the degree to which it can increase its financial resources to respond to rising commitments by either expanding its revenues or increasing its debt. A government meets the test of flexibility when it can respond to changing economic conditions such as a recession or higher interest rates without making substantial changes to the way it operates.

1.27 A government's net debt and debt charges provide insight into whether it can respond to rising commitments without increasing its revenues. A rising debt burden and debt charges indicate there are fewer resources to allocate to programs and services.

1.28 One measure of a government's flexibility is the interest costs as a percentage of total revenues. This is sometimes referred to as the "interest bite." In 2007-08, debt charges on government borrowings were $118.9 million. The trend in the interest bite is shown in **Exhibit 1.7.**

EXHIBIT 1.7
INTEREST COSTS AS A PERCENT OF REVENUE



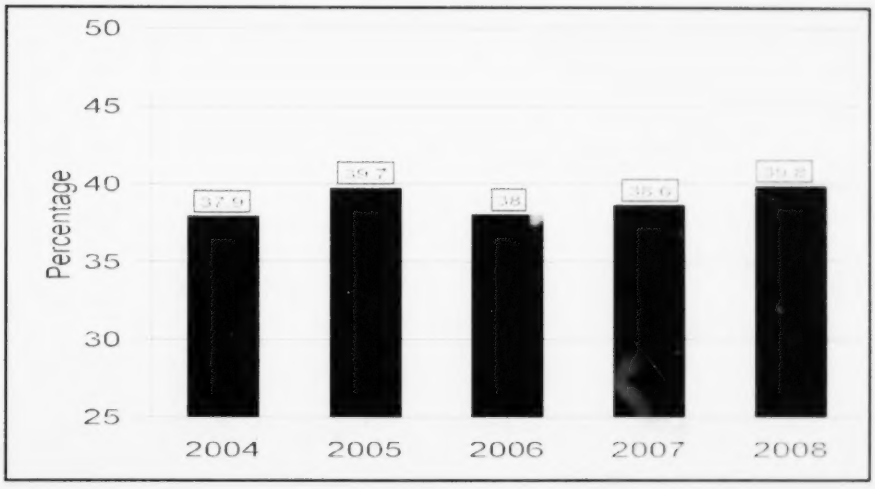
1.29 As indicated in **Exhibit 1.7**, the interest bite has not changed significantly from 2004. Our net debt is over a billion dollars and the first $118.9 million must be earmarked to pay interest costs and is unavailable for government programs. Recent debenture issues have been for 30 year terms at comparatively low interest rates.

Vulnerability

1.30 Vulnerability is the degree to which a government is dependent on, and therefore vulnerable to sources of funding outside its control or influence. In 2007-08, the Federal Government provided revenue of $518 million to the Province, an increase of $43.5 million from

2006-07. The trend in federal revenues relative to total revenues for the last five years is shown in **Exhibit 1.8.** This exhibit shows that approximately 39.8 cents of each dollar of revenue received by the Province in 2007-08 came from the federal government.

EXHIBIT 1.8
FEDERAL REVENUE AS A PERCENT OF TOTAL REVENUE



1.31 Revenue from provincial sources is more controllable through measures such as provincial tax legislation or adjustments in user fees. Federal transfers are subject to different variables such as federal fiscal policies and the performance of other provincial economies. Any federal fiscal policy change impacts the Province.

SUMMARY

1.32 It is important for Members of the Legislative Assembly to have a regular update on the financial condition of government. This section provides summary information using indicators recommended by the Canadian Institute of Chartered Accountants. The indicators provide useful insight into government's ability to sustain its programs, the flexibility it has to respond to economic changes, and its vulnerability to sources of outside funding. The indicators help to put the finances of government into perspective and assist Members to understand and interpret the information.

1.33 Further to the above discussion, we recognize that there are other relevant non-financial matters which have to be taken into consideration by Members of the Legislative Assembly in making budgetary decisions and setting government policy direction.

SPECIAL AUDITS AND EXAMINATIONS

2. INTRODUCTION TO SPECIAL AUDITS AND EXAMINATIONS

AUDIT PROCESS

2.1 Subsection 13(2) of the Audit Act states that the Auditor General may conduct any audit or examination considered necessary to determine whether any agency of government is achieving its purpose, is doing so economically and efficiently and is complying with the applicable statutory provisions.

2.2 Due to the size of our Office and the complexity and magnitude of government operations, we cannot audit all Government programs on an annual basis. There are numerous factors that influence the preparation of our annual audit program: the results of previous audits, the total revenues and expenditures at risk, the complexity of operations of the entity, the significance of potential issues that may be identified by an audit, and the impact of the program on the public.

2.3 Special audits and examinations are conducted in accordance with standards established by the Canadian Institute of Chartered Accountants. There are three distinct phases in these types of audits. In the planning stage, audit staff obtain a thorough knowledge of the auditee organization or program and the environment in which it operates. This knowledge is obtained from a variety of sources and is used to develop an audit plan which contains the purpose, objectives, scope, and timing of the audit. During the second, or implementation stage, the auditor performs tests and gathers sufficient appropriate audit evidence which is then evaluated and analyzed. In the third stage, a report is drafted which includes audit observations and recommendations. The auditee is provided with a copy of the draft report for discussion purposes. At the conclusion of the audit, a final report is issued to the department or agency and a written response is requested from management.

2.4 We provide the auditee with recommendations to address any problems identified. The authority and obligation to implement changes to deal with these problems remain with management. As auditors, our primary concern is that action is taken to address issues raised during the audit.

2.5 Under Section 16 of the Audit Act, the Auditor General is required to call attention to any matters which he considers necessary to be brought to the attention of the Legislative Assembly. This report provides information on the following special audits and examinations: Provincial Nominee Program - Immigrant Partner Category, In-Province Physician Payments, Department of Social Services and Seniors - Grants to Non-Government Organizations and Government's Involvement With Natural Organic Food Group PEI Inc.

3. PROVINCIAL NOMINEE PROGRAM - IMMIGRANT PARTNER CATEGORY

OVERALL COMMENTS

3.1 The Immigrant Partner Category of the Provincial Nominee Program has had a significant impact on the Island economy. Through this Program Island businesses have had access to approximately $120 million in investment capital in the last two years. In this report, we present a number of findings and recommendations related to the administration of the Program by Island Investment Development Inc. (IIDI).

3.2 The Program was established pursuant to the Federal Provincial Cooperation Agreement on Immigration and is subject to the Immigration and Refugee Protection Act Regulations. Due to impending regulatory changes, a decision was made by IIDI to process as many applications as possible prior to the implementation of the new regulations. As a result, the volume of applications processed from April 1, 2008 to September 2, 2008 increased significantly.

3.3 The Board of Directors of IIDI did not provide sufficient oversight given the significance of the Program to overall corporate operations. Over the period, a number of Program policies were developed and implemented without documented approval or authorization by the Board of Directors of IIDI and the Corporation did not provide information on this Program in its Annual Report to the Legislative Assembly.

3.4 There were a number of elected officials and senior government officials who had ownership in corporations that received investment capital under the Program. The question of conflict of interest in these situations has been raised. Our review has highlighted the limitations and ambiguity in the Conflict of Interest Act and the Treasury Board Conflict of Interest Guidelines.

3.5 When the Federal regulatory changes were implemented on September 2, 2008, the PEI Immigrant Partner Category was suspended. There are 2,281 immigrants that have been nominated

by PEI who are awaiting Federal approval as of January 31, 2009. Some of these applicants will be declined at the Federal level and will be seeking a refund of their investment. While there are rejected investor trust funds, it is not clear whether the funds on deposit will be sufficient. There is a potential liability issue in terms of both amount and responsibility which needs to be addressed.

3.6 Businesses received substantial funds under the Program based on business plans submitted. IIDI has not determined whether the funds were used as intended. There is a need to develop a strategy for follow-up.

3.7 IIDI has not carried out an evaluation of this Program to determine whether it is achieving the results intended. The immigrants we interviewed raised a number of concerns. Due to increased Program volumes in 2008, there is an expectation of an increased number of immigrants arriving in PEI over the next few years. A Provincial Strategy is needed to improve settlement and retention services on a go forward basis.

3.8 Based on the complexity of the Program and the public interest in this area, our report contains additional explanatory information. A number of our recommendations deal with broad issues while others are more relevant if a new program is implemented based on the Federal regulatory changes effective September 2, 2008.

BACKGROUND

3.9 In 2001, PEI entered into the Federal Provincial Cooperation Agreement on Immigration. The purpose of the Agreement was to develop a partnership between the Federal and Provincial governments on recruitment, selection, admission, settlement and integration of immigrants to Prince Edward Island. The Agreement allowed for some delineation of roles and responsibilities including sharing of information and cooperation on planning and policy development.

3.10 Under the Cooperation Agreement the Province established the Provincial Nominee Program with the following objectives:

a) to admit provincial nominees to Prince Edward Island whose admission is consistent with the Province's immigration policies and which will support the industrial and economic goals of Prince Edward island;

b) to admit to Prince Edward Island those immigrants nominated by the Province and their qualifying dependents; and

c) to process provincial nominees nominated by Prince Edward Island for permanent residence as expeditiously as possible, taking into account statutory requirements, operational and resource constraints, and service standards as developed.

3.11 Under this Agreement the Province is responsible for developing criteria, assessing applicants against those criteria and making a formal nomination to the Federal authorities. The Federal government continues to be responsible for determining the admissibility of each nominee with respect to all Federal legislative requirements including health, criminality and security.

3.12 There are four categories of applicants under the PEI Provincial Nominee Program (PNP):

- **Immigrant Partner** - where a principal applicant proposes to make an investment in a PEI company and take an active role in that company as a director or senior manager.
- **Immigrant Entrepreneur** - where a principal applicant proposes to establish a viable, new business on PEI.
- **Immigrant Connections** - where a principal applicant suggested by a PEI based "champion" meets settlement and employability criteria.
- **Skilled Worker -** where a principal applicant with specialized skills and experience fills a labour market need on PEI.

3.13 Island Investment Development Inc. (IIDI) is responsible for the delivery of economic related immigration programs on behalf of the Province. IIDI is a provincial Crown Corporation under the Ministry of Innovation and Advanced Learning. The objectives of the Corporation are to raise capital in foreign and domestic markets, to provide investment opportunities in projects of significant economic benefit to

the Province, to promote the Province as a destination for offshore investment, and to attract entrepreneurial expertise to the Province.

3.14 **Exhibit 3.1** illustrates the number of applications approved by IIDI since 2001.

EXHIBIT 3.1
PROVINCIAL NOMINEES
FROM PROGRAM INCEPTION TO SEPTEMBER 2, 2008

Year ended March 31	Immigrant Partner	Skilled Worker	Immigrant Entrepreneur	Immigrant Connections	Total
2001-02	2	5	0	0	7
2002-03	50	15	6	0	71
2003-04	62	24	9	0	95
2004-05	98	30	6	0	134
2005-06	215	30	3	0	248
2006-07	368	53	5	81	507
2007-08	750	34	11	28	823
2008-09 to November	1,877	29	0	7	1,913
Total	**3,422**	**220**	**40**	**116**	**3,798**

3.15 The majority of nominations have been made through the Immigrant Partner Category and that is where we focused our audit. The PEI Immigrant Partner Category has been very popular in foreign countries. Key selling points of the Program for the immigrants include the favorable processing time relative to the Federal Program and the well defined eligibility criteria.

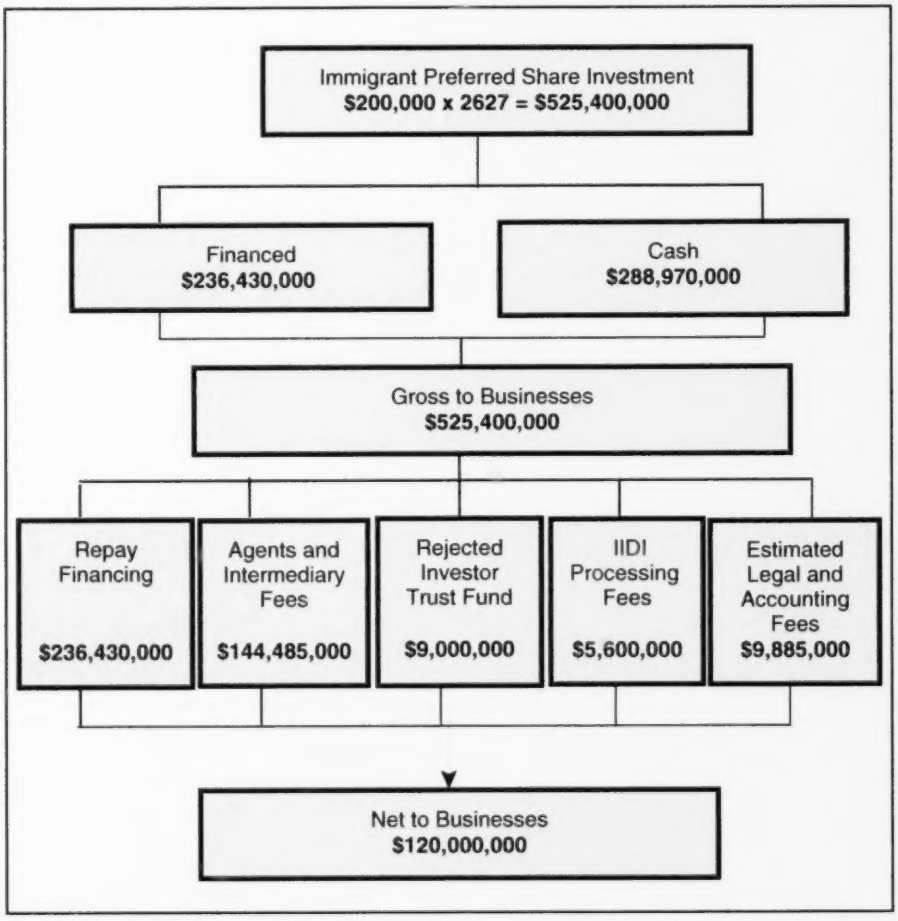
3.16 The Program details were revised and approved by Executive Council in 2002. Under the Immigrant Partner Category an immigrant who has a net worth of at least $400,000 makes a $200,000 preferred share investment in an eligible Island business and takes on a role as a director or senior manager of the company.

3.17 Financing of a portion of the investment is allowed. The financing structure in place varies, but in general the immigrant pays $110,000 and borrows $90,000 to make the preferred share investment of $200,000. The shares, as well as any dividends to be received, are pledged as security for the loan. The immigrant foregoes any return on the investment.

3.18 From the $110,000 received from the immigrant an intermediary pays an immigration agent in the foreign country, retains a portion as a fee and passes on net proceeds of approximately $55,000 to the Island business. The business pays legal and accounting expenses, IIDI processing fees and in some cases a contribution to the Rejected Investor Trust Fund. **Exhibit 3.2** illustrates the theoretical flow of funds for fiscal years 2007-08 and 2008-09 based on 2627 investment units and using the following assumptions:

- $90,000 financed portion in each case;
- $55,000 proceeds to the business after agent and intermediary fees; and
- legal and accounting fees of approximately $3,800 per investment unit.

EXHIBIT 3.2
THEORETICAL FLOW OF FUNDS
FISCAL YEARS 2007-08 AND 2008-09



3.19 Financing is used in some other provincial programs and the Federal program. We were advised that without a financing structure the Program would not be marketable in foreign countries.

3.20 The Regulations for the Federal Immigration and Refugee Protection Act (IRPA) prohibit any provincial arrangement whereby the immigrant is said to be making a passive investment. Selection on the basis of the ability to invest capital without involvement in the management of the recipient business is exclusive to the Federal program. In 2002 when the Program details were approved, there was

discussion and concern expressed by Federal officials regarding the definition of a passive investment and whether the financing structure and program details for the PEI Nominee Program were a violation of the regulations. The Federal government processed nominations from PEI at all Embassies from 2002 until 2008. On March 8, 2008 the Federal government published regulatory text indicating proposed amendments to the Immigration and Refugee Protection Act Regulations. These amendments would significantly alter the requirements of the PNP. In addition to other provisions, these regulation changes require the immigrant to make a minimum $1 million equity investment in the business or control at least 33 1/3 percent of equity in the business.

3.21 There was considerable discussion among Provincial and Federal officials as to the effect of these amendments on the PNP. These regulations were to become effective September 2, 2008. At the time of the announcement there were 1,000 immigrant applications in process at IIDI. A decision was made by IIDI to process as many immigrant applications as possible up to the implementation date of the regulations. The total nominations approved in 2008-09 up to September 2, 2008 was 1,877.

3.22 The Immigrant Partner Category of the PNP was suspended in 2008, and as of January 31, 2009, 2,281 nominees are awaiting Federal approval under the old regulations.

OBJECTIVES AND SCOPE

3.23 In accordance with Section 13 of the Audit Act we conducted a value-for-money audit on the Immigrant Partner Category of the Provincial Nominee Program.

3.24 The objectives of the audit were as follows:

- To determine whether management controls existed to ensure that approved immigrant partner applications and business applications were assessed in accordance with established policy and whether adequate documentation existed to support the assessment;

- To determine how the intermediaries were approved to operate on PEI and whether it was an open process;
- To determine whether the Province was in compliance with key aspects of the Federal Provincial Cooperation Agreement on Immigration; and
- To determine whether the controls over the receipt and disbursement of immigrant deposits existed, were operating as intended and met the policy requirements.

3.25 In conducting our audit we focused on applications processed during calendar years 2007 and 2008 because 81 percent of the nominations occurred in that time period. Our procedures included examination of business application files and supporting documentation, examination of immigrant application files and supporting documentation, as well as an assessment of immigrant deposit receipts and disbursements. We carried out extensive interviews with senior government officials, intermediaries, immigrants, an official of the Federal government, as well as several other stakeholders. In addition we reviewed numerous pieces of legislation and regulations at both the provincial and federal levels as well as documents, correspondence and consultants' reports from various sources.

3.26 Our examination was conducted in accordance with the standards for assurance engagements encompassing value-for-money established by the Canadian Institute of Chartered Accountants and accordingly included such tests and other procedures as we considered necessary in the circumstances.

DETAILED AUDIT OBSERVATIONS

Program Development and Authorization

3.27 Island Investment Development Inc. is a Crown corporation established pursuant to the Island Investment Development Act. Under the Act, the affairs of the corporation are to be conducted by a Board of Directors which is responsible for the general management and operations of the corporation. The Board consists of the Deputy Minister of Innovation and Advanced Learning (formerly Development

and Technology), the Deputy Provincial Treasurer, the Deputy Minister of Tourism, and the Executive Director of the Corporation. At the program administration level, there are two program directors and a number of program and financial officers.

3.28 As the governing body of the Crown corporation, we expected the Board of Directors of IIDI to exercise oversight over the Program. Over the last several years the activity in this Program has made it one of the most significant programs delivered by IIDI, accounting for hundreds of millions of dollars in deposits and tens of millions of dollars in fee revenues. We were advised that historically the IIDI Board of Directors deals mainly with lending issues. A review of the minutes of the meetings of the Board of Directors confirmed that Program changes, policies, and approvals were not discussed or approved at the Board level.

3.29 In 2002 Executive Council approved a framework which laid out the details of the Provincial Nominee Program. Because of the need to respond to expected demand for the Program and changing market conditions, Executive Council approved that on a go forward basis policy changes would be made at the Ministerial level as opposed to requiring Executive Council approval.

Policy Changes

3.30 We expected policy changes to be approved at the Ministerial level as approved by Executive Council or at the Board of Directors level. We found that most Program policy changes did not have documented approval. We were advised that the majority of policy changes were discussed with the Deputy Minister of Innovation and Advanced Learning but approval was rarely documented.

3.31 From the perspective of IIDI in administering the program, there are two approval streams: assessment of the immigrant applications and assessment of the business applications. During the first several years the Program was in operation, the number of immigrant applications was limited. Although there were some policy changes particularly in the extent of supporting documentation

required, most policy requirements for the immigrant applications were consistent throughout the period.

3.32 For the business applications stream, however, there were a number of significant policy revisions. In the first several years of the program, all that was required of the business applicant was a letter requesting approval under the program and if the business was in one of the eligible sectors approved by Executive Council, it would be approved for four units. **Exhibit 3.3** shows the Ministry's strategic priority sectors and excluded sectors that were in place at the beginning of the Program.

EXHIBIT 3.3
STRATEGIC PRIORITY SECTORS AND EXCLUDED SECTORS
AS OF AUGUST 2002

PRIORITY	EXCLUDED
Aerospace	Primary Resources: agriculture, fishing, forestry
Manufacturing and Processing	Retail
Life Sciences	Wholesale
Bio-Resource Development	Financial Services
Tourism Attraction	Professional Practice
Tourism Fixed Roof Accommodations (excluding cottage development)	Real Estate
Information and Communication Technology	Construction
Film, Television and New Media	Business and Personal Services
Peer Reviewed Exportable Technology	

3.33 As the Program increased in volume, IIDI made a number of policy changes related to the eligibility of business sectors. The sectors were expanded to include retail and restaurants with certain conditions, community care facilities, start up companies and capital intensive service industries. Later the number of units the business would be eligible for was based on established criteria including an assessment of the cumulative inventory, fixed assets and wages paid. In addition, there were numerous other policy changes which were implemented and applied by IIDI staff when assessing the applications received from businesses. Changes to the policies regarding the eligibility criteria for Island businesses had a significant

impact on the Program. These changes affected which businesses could be eligible to receive investment units.

3.34 By the end of 2006, IIDI required financial statements and projections to assist in the assessment of eligibility. Due to the high volumes near the end of the Program, some policy changes were made to reduce the amount of workload for the businesses and the accountants involved in the preparation of business applications.

3.35 Another key policy change included the requirement set in October 2006 that each business receive at least $55,000 from each unit under the financing structure. Up to that point there were wide variations in the net amount available to the business from each unit. In October 2007, IIDI implemented a policy requiring each company to sign a Use of Proceeds Agreement whereby the business made a commitment to use the proceeds within two years in accordance with the business plan or as stated in the Agreement. If it did not, the business could have to pay a penalty of $55,000 per unit. In January 2008, the cumulative investment policy was relaxed. The policy had restricted the number of units a shareholder could receive through affiliated and related companies.

Application Approvals

3.36 Under the IIDI Act the Executive Director is responsible for the day to day administration of the affairs of the Corporation. We expected the Executive Director to be actively involved in the operation of the Program and that there would be a clearly documented process for decision making on nominee and business applications. We found the highest level of documented approval for applications was the Program Director. The authorization of the Executive Director pursuant to the IIDI Act was never formally delegated to a Program Director. In addition, we were advised by the Program Director that exceptions to policy when they arose were discussed with the Deputy Minister of Innovation and Advanced Learning but approval was not documented. The need for a clearly documented process on business approvals became even more important when the Deputy Minister was changed at a critical point

prior to the suspension of the Immigrant Partner Category of the Program.

Communication

3.37 In general, PNP policies were available on the IIDI website. We were advised that as policy changes were made the website was updated and the approved intermediaries responsible for matching the immigrants to the businesses were informed directly by IIDI.

3.38 Generally we observed that the policies described on the website in the fall of 2008 reflected the policies that were in effect at that time. We did, however, note a few discrepancies. From the outset of the Program there was a policy limiting each approved business to four investors at one time. The limit of four investors to each business would include wholly owned subsidiaries or affiliated companies where 50 percent or more of the common shares were held by a single shareholder or a beneficiary company. In January 2008, this policy was no longer enforced and the eligibility section of the website was updated with a statement that, where there are common shareholders between multiple businesses seeking access to the Program, IIDI reserves the right to limit access to further units if one purpose of the company structure is to access further units. This decision would be at the sole discretion of IIDI. However, the original detailed policy on restrictions on cumulative investment remained on the website.

3.39 In July 2008 a decision was made to open up a new sector: capital intensive service businesses. A notification of this change in policy was e-mailed to intermediaries and accountants in public practice. However, the listing of eligible sectors under the Program was not updated on the website. In addition, we noted that not all public accounting firms were notified.

3.40 A basic tenet of government administered programs is that all qualifying applicants have an equal opportunity to apply. Where policies were inconsistent or not complete it could be difficult for potential business applicants to determine whether they would qualify under the program.

3.41 In relation to immigrant eligibility, the requirement for management or business ownership experience was reduced from five years to three. We noted that this change was implemented but was not posted on the website.

Recommendations

3.42 The IIDI Board of Directors should fulfill its responsibility to provide oversight for all operations of IIDI including the Provincial Nominee Program.

3.43 Program policies should be documented and approved by the Board of Directors of IIDI.

3.44 IIDI should ensure that approved eligibility criteria and policies of the Provincial Nominee Program are accessible to all potential applicants.

Immigrant Applications

Background

3.45 When people decide to emigrate from their country of residence, they usually seek out the assistance of a professional immigration agent to assist them in selecting the appropriate immigration program and to assist with preparing their applications. Among other things, PEI's program requires that each agent be a member in good standing of the Canadian Society for Immigration Consultants (CSIC), or be a lawyer in good standing of a Canadian law society, and register with IIDI through the filing of agent profile and code of conduct forms. Given the competitive nature of the industry, agent compensation must be competitive to encourage agents to promote the PEI program. Agents forward immigrant applications to one of seven approved intermediaries who check the information for completeness before forwarding the documents to IIDI for review.

3.46 Applicants must submit various Federal and Provincial immigration forms along with supporting documentation proving that

they meet the Program's eligibility criteria. The key provincial immigrant eligibility criteria established under the PNP required the immigrants to:

- Have a minimum net worth of $400,000 Canadian dollars;
- Make a $200,000 investment by way of preferred shares in an eligible Prince Edward Island company;
- Become a director or senior management employee in the investee company;
- Be an applicant between the ages of 21 and 49 and no older than 55;
- Have a minimum 12 years of education (high school); and
- Have at least 3 (previously 5) years of management or business ownership experience in a sector with relevance to the Prince Edward Island economy.

3.47 Provincial Nominee Program officers reviewed immigrant applications and assessed the information against the eligibility criteria. If the applicant met the criteria, he or she was invited to PEI to participate in an interview with Program staff. The focus of these interviews was to clear up any questions on the applicant's file, obtain further documentation to support the various claims made in the application such as net worth and work experience. The interview was also used to assess the immigrant's proficiency in speaking and understanding English. During the spring and summer of 2008, these interviews were held overseas in Hong Kong and Dubai to reduce the processing time.

3.48 After the interview, PNP staff performed a final review on the eligibility of the immigrant. IIDI sent notice to the immigrant, to his or her agent, and the intermediary indicating that the applicant was accepted into the Program. At this point, the applicant was requested to make a $25,000 good faith deposit and, if necessary, a $20,000 language deposit. The applicant's final step was to make a preferred share investment of $200,000 in an eligible PEI company. This investment was facilitated by one of the Program's approved intermediaries.

3.49 When the immigrant nominee decided on his or her investment, the intermediary sent the complete package of investment documents to PNP staff for a final review. If PNP staff were satisfied with the details of the investment documents, they would prepare the file for nomination. Prior to nomination, PNP staff would confirm that the net proceeds of the investment were released to the company. The Provincial Director of Immigration would then print a formal nomination certificate and send it to the Canadian Embassy in the immigrant's country of residence. Correspondence was sent to the immigrant advising him or her of the next steps to secure a permanent resident visa. The immigrant nominee had one hundred and eighty days to provide all the necessary documentation to the Federal government.

Procedures Carried Out

3.50 We selected a sample of approved nominee files and examined documentation to determine whether the applicant had been assessed against the eligibility criteria and that the necessary documentation existed in the file to support the application. Our sample was selected from calendar 2007 and 2008 files.

3.51 We also examined a sample of good faith and language deposit receipts and refunds during calendar 2007 and 2008 to assess the controls and procedures in place. For deposit receipts, we assessed the procedures in place to ensure that deposits were collected, deposited to IIDI's bank account on a timely basis, and accurately recorded in IIDI's accounting records and in the Program's database. For refunds, we looked to see that adequate documentation existed to support the payment in accordance with the policy, that proper signatures existed to authorize the payment, and that the payment was for the correct amount.

3.52 In addition, we interviewed a sample of immigrants to obtain information on their experience with the Program. The results of these interviews are discussed in a later section of this report.

Results of Examination

Nominee Files

3.53 Based on our review of applicant files and interviews with PNP staff, we found no significant issues to report regarding the assessment of immigrant applications. We found that IIDI had controls and procedures in place to assess immigrant files for eligibility and appropriate documentation was obtained to support the approval.

Deposit Receipts and Refunds

3.54 The magnitude of the good faith and language deposits held by IIDI has increased with the increased volume of activity under the PNP program. **Exhibit 3.4** shows the balances held on deposit in recent years.

EXHIBIT 3.4
ISLAND INVESTMENT DEVELOPMENT INC.
AMOUNTS HELD ON DEPOSIT
($000)

	Audited 2005-06	Audited 2006-07	Audited 2007-08	Unaudited Jan 31/09
Good Faith Deposits	$10,201	$18,760	$36,254	$ 74,775
Language Deposits	2,871	8,532	19,743	46,000
Total	**$13,072**	**$27,292**	**$55,997**	**$120,775**

3.55 We were advised that the intention of the Good Faith Deposit Agreement has never changed, rather the internal procedures used to determine whether the terms of the agreement have been met have evolved over time. PNP staff recognize that communication regarding the good faith deposit has been less than ideal, and they are taking steps to improve the process including having a more formalized policy document, translating it into various languages, and implementing communication up front when immigrants come to PEI

to outline what exactly will be required in terms of supporting documentation for a refund.

3.56 For language deposit refunds, it appears that the lack of communication on the refund process has caused more concern than the changes themselves. The requirements for language proficiency have not changed; an immigrant must obtain a moderate proficiency for each of the following: reading, writing, speaking, and listening. One change dealt with who would be conducting the English evaluation and how that evaluation was reported to IIDI. This change caused confusion over the level of proficiency required to receive a refund. Prior to December 2008, the evaluation was conducted by the English as a Second Language (ESL) instructors. These instructors would send a letter to IIDI indicating the level of proficiency achieved. A reported level of 3 meant that the immigrant had completed level 3. Subsequent to December 2008, the evaluation was conducted by the PEI Association for Newcomers (ANC). This Association provided IIDI with a mark for the proficiency reached. ANC noted a score of 4 meaning that the immigrant had completed level 3 and was now eligible to be placed at level 4. This led to confusion in the immigrant community that the requirements were changed from level 3 to level 4. We were advised that immigrants were told of these changes through the ESL instructors. Since December 1, 2008 ANC has provided information to the immigrants on the changes to the marking structure.

3.57 Another issue related to the language deposit refund was the fact that demand for English classes began to far outweigh the number of federally and provincially funded seats available. As such, immigrants were being put on a waiting list. Immigrants expressed concerns that they would not receive their language training in time to meet the one year requirement for the language deposit refund. PNP staff informed us that as long as an immigrant was on a waiting list, they would be granted an extension to meet the language requirement.

3.58 Based on our testing of deposit receipts and refunds, controls exist to ensure the accurate and complete processing of transactions. Documentation is required to support the transactions and an

approval process is in place. Our work substantiated the concerns raised by the immigrants we interviewed, notably that documentation requirements to support a refund were expanded and that these changes were not well communicated.

Recommendation

3.59 IIDI should take steps to improve communication with immigrants regarding good faith and language proficiency deposits and refunds.

Business Applications

Background

3.60 Nominees were required to make a preferred share investment in an eligible Island business prior to being nominated under the Program. As the Program evolved between its inception in 2001 and the fall of 2008, IIDI implemented new policies and controls over the business eligibility criteria to manage the expanding Program. Island Investment Development Inc. ceased accepting business applications under the Immigrant Partner Category on July 31, 2008 then subsequently reopened receipt of applications for two days on August 5 and 6, 2008. **Exhibit 3.5** provides statistics on business applications from inception to February 2009.

EXHIBIT 3.5
INVESTMENT STATISTICS
FROM PROGRAM INCEPTION TO FEBRUARY 2009

Number of Businesses That Received Units	1,423
Number of Actual Investment Units Matched	3,374

3.61 When a company was deemed eligible by IIDI, it received an eligibility letter, valid for one year, that outlined the terms of the approval including the number of investor units it was eligible to receive and any conditions. Company officials were then instructed to bring the eligibility letter to one of the seven approved investment

intermediaries who would be responsible for matching the business with a nominee.

3.62 When a nominee and business were matched, the necessary legal documents were signed and sent to IIDI for final approval. PNP staff confirmed with the company's lawyer that the funds were disbursed to the company and then issued a nomination certificate for the immigrant.

Examination of Files

3.63 We selected a sample of approved business applications from 2007 and 2008 calendar years. For any MLA since the inception of the Program we examined any related business applications submitted while he or she was a Member. For any employee at the Deputy Minister level in calendar year 2007 and 2008, we examined any related business application submitted while he or she was employed. Finally, we reviewed a sample of businesses that were approved under the "special small valued added" business class. We looked to see whether business applications were assessed in accordance with established policy, whether the business application file included the necessary forms and analyses supporting the decision to accept, and whether controls existed to ensure that funds disbursed were used as intended in the company's business plan.

3.64 We also selected a sample of rejected files from 2008 to ascertain whether the eligibility criteria were properly applied and that appropriate documentation existed to support the decision to decline the business for eligibility under the Program.

Results of Examination

Application of Policy

3.65 We found that the business applications we reviewed were generally assessed in accordance with established policy and eligibility criteria, although we did note some deficiencies. Specifically, we noted instances where senior officials directed approval on eligibility, where restrictions on related party entities were not adhered

to, and where a business received more investment units than was approved.

3.66 We expected exceptions to policy to be supported by documented approval of the Executive Director or Board of Directors giving more credibility and transparency to the business approval process. We noted five business files that were approved where staff advised they were directed to approve them. There was no documented approval above the Program Director level.

3.67 Three of these companies were professional services companies, which are ineligible under the program criteria. One was a consulting firm, one was a physiotherapy clinic, and one was a start up company offering settlement and retention services to immigrants upon their arrival in PEI. The consulting firm was approved for one unit on the basis that it's proposed expansion would serve the Island well, in particular with regards to the bio-science sector. The physiotherapy clinic was approved for one unit on the basis of the 2009 Summer Games scheduled for the Island. The settlement and retention business was approved for four units on the basis that it complemented the PNP.

3.68 Two of the companies were not-for-profit entities, which are ineligible under the program criteria. Both of the companies set up a for-profit subsidiary to qualify under the terms of the Program. One of the organizations produces theatrical performances. This company was approved for four units on the basis that it was important to the tourism industry. It was noted in the file that this organization already received significant annual funding from government sources under other programs. The other organization was hosting a concert in the fall of 2008 and was approved for four units on the basis that the event was important to Island tourism, especially in the shoulder season. This organization was not matched with immigrant investors before the Program was suspended in September 2008.

3.69 In addition to our sample items there were seven instances brought to our attention where concerns were raised by PNP staff and the Deputy Minister at that time regarding business eligibility.

However, in each case they were directed to provide approval for four units.

3.70 Prior to January 2008, PNP policy restricted the number of units that were accessible to related businesses. We noted three instances where businesses were approved for units prior to January 2008, where PNP staff did not adhere to the restrictions under the related parties policy.

3.71 We noted one instance, due to an administrative error, where a company received three investor units, but was eligible to receive only two units.

Recommendation

3.72 The Board of Directors of IIDI should establish a policy on approval levels required for business applications and exceptions to policy.

Documented Support

3.73 In general, we found that the business application files we reviewed had the necessary analysis and documentation to support the decision to approve the business' application, although we noted a few discrepancies. Specifically, we found instances where no evidence existed to demonstrate that terms of conditional eligibility were verified prior to the business receiving units, one instance where the documentation on file did not support approval, and one instance where the number of eligible units was not supported by any rationale.

3.74 Three businesses in our sample were approved for eligibility based on certain conditions being met. One file was approved on the condition that the owners were to make an additional cash injection of $130,000; one file was approved on the condition that the business provide evidence of third party financing in the amount of $20,000; and one file was approved on the condition that evidence be provided on the redemption of the existing preferred share units that had been issued over five years ago under the Program. Based on our review of the files and discussions with PNP staff, there was nothing in the

files to support that the conditions had been met. In all three cases, PNP staff obtained the appropriate supporting documents after we requested the information. As such, we could not conclude whether IIDI had verified that the terms of the conditional eligibility were met prior to approving the investment transaction.

3.75 One file in our sample was in serious financial difficulty but was approved as eligible and received four investment units. We noted that the documentation on file indicated that without the PNP investment it would be facing bankruptcy. There were no historical financial statements provided with the business plan. The file included a business plan with a marketing strategy, however, there was also a letter prepared by the accountant which included a schedule of disbursements to be made from the proceeds of the PNP units. All of the proceeds were directed to paying down overdue creditors with no residual to be used to implement the business plan. One of the conditions for approval under the program was for an attestation that the company was up to date on all Federal and Provincial remittances. We noted that this company owed over $60,000 in sales tax and property tax. These taxes were paid out of the proceeds.

3.76 There was one instance where a company was approved for two units, but the number of eligible units was not based on any documented rationale, and there were no financial statements or financial projections which would substantiate the number of units approved.

Recommendations

3.77 IIDI staff should verify that the terms of conditional eligibility requirements are met before processing the file.

3.78 IIDI should ensure that required documentation is on file to support the business approval.

Declined Business Applications

3.79 In general, we found that for the declined business files we reviewed, the eligibility criteria were properly applied and appropriate

documentation existed to support the decision to decline the business for eligibility under the Program. We noted one inconsistency in our review.

3.80 Companies that applied under the capital intensive service category, created towards the end of the Program, were required to meet certain minimum dollar thresholds: one for capital assets plus inventory and one for wages. One company was declined because it did not meet the capital asset test to qualify for units. We noted that PNP staff did not consider the fact that the company had claimed to have purchased $95,000 worth of capital assets since the year end financial statements sent as part of the application package. We had seen in other files where applicants were asked for receipts to substantiate claims of additional purchases and such capital additions were taken into consideration when calculating business eligibility. In this case, the capital asset test was prepared on the basis of the financial statement information only and did not consider the additional purchases of $95,000 which would have resulted in the business meeting the eligibility requirement.

Recommendation

3.81 IIDI should ensure business files are subject to consistent application of the eligibility criteria.

Implementation of Use of Proceeds Agreement

3.82 IIDI has not followed up to determine whether the investment proceeds have been used in accordance with the business plan supporting eligibility. In October 2007, IIDI implemented a Use of Proceeds Agreement to be signed by all eligible companies accepted into the Program. The wording of the Agreement states that the shareholders commit to use the investment proceeds in accordance with the business plan. Further, the Agreement states that if the shareholders do not use the funds within two years as intended in the Agreement, they could be charged a penalty of $55,000 per investment unit received.

3.83 We were advised that IIDI is currently in the process of developing an approach to follow up on the Use of Proceeds Agreements on a go forward basis. The initial files subject to the Use of Proceeds will be due in the fall of 2009.

3.84 Prior to October 2007, there was no Use of Proceeds Agreement in place. However, there was an undertaking by the investee company to IIDI and to the nominee stating that the funds would be used as intended in accordance with the business plan. A file was brought to our attention where the proceeds were used for other purposes and the intended business was not established. In general, IIDI has a responsibility to follow up and obtain information to determine whether Program funds were used as intended. The undertaking would allow IIDI to request information on businesses which would be useful in evaluating the success of the Program.

3.85 Program policy requiring the Use of Proceeds Agreement was implemented in October 2007. The implementation of this Agreement is an important policy change as it permits IIDI to follow up with businesses and charge a penalty for noncompliance. We expected Use of Proceeds Agreements to be on file for investments after October 2007 and that the wording of the Agreement would be consistent with policy and accurate with regards to the specific details of the business application.

3.86 We found three instances where no Use of Proceeds Agreement had been signed related to investment documents approved by IIDI subsequent to the implementation of the policy in October 2007.

3.87 We noted two business applications where the business plan and accompanying financial projections demonstrated that proceeds would be used to pay off shareholder or related party debt. In one of these instances, there was no Use of Proceeds Agreement as reported above. In the second instance, the Use of Proceeds Agreement existed, but it did not explicitly prohibit payments to shareholders.

3.88 We noted additional inconsistencies in the wording of certain Agreements. Specifically, we noted two instances where the wording of the Agreement was inconsistent with the uses reported in the company's business plan.

Recommendations

3.89 IIDI should develop a strategy to follow up on businesses which received units under the Program. IIDI should provide information in its Annual Report on the results of these follow-up procedures.

3.90 IIDI should ensure, on an ongoing basis, that all companies sign the Use of Proceeds Agreement, and that the wording of all such agreements prohibits payments to shareholders.

Other Matters of Note

3.91 The investment documents are the legal documents that support the investment. We noted some errors in the investment documents in our sample of files. For example, we noted one instance where the business plan submitted was more than five years old and did not reflect the business' current situation although up-to-date financial statements were submitted. We also noted one instance where the business plan was missing, one instance where the business plan omitted part of the company's operations, and one instance where information in the investment documents was for a related company applying for units.

Recommendation

3.92 IIDI should be diligent in the review of investment documents to identify errors and omissions.

Intermediaries

3.93 The financial intermediary plays a key role in the operation of the Provincial Nominee Program by bringing together the approved businesses and the nominees. The intermediary develops a relationship with a number of agents in foreign countries. These agents send files to the intermediary for immigrants who are interested in moving to PEI. The intermediary performs a preliminary review of the immigrant files received from the agent and forwards these files to IIDI for approval.

3.94 At the same time, eligible Island businesses make application to IIDI for approval to receive units under the Program. When IIDI completes its assessment of the business applications, it provides the business with an eligibility letter. When the business is approved as eligible, it will approach an intermediary to begin the process of being matched with immigrants.

3.95 The intermediary promotes the business to an immigrant and obtains his or her agreement to invest in that company. When the immigrant is matched with an eligible business, the intermediary ensures the legal investment documents are completed as required and submits them to IIDI for review prior to the nomination of the immigrant.

3.96 As indicated the intermediary arranges financing which facilitates the marketability of the program. There are variations in the financing structure offered by different intermediaries. **Exhibit 3.6** illustrates examples of three financing structures that were in place.

EXHIBIT 3.6
INTERMEDIARY FINANCING STRUCTURES

Structure 1	Structure 2	Structure 3
Immigrant cash $110,000 Immigrant borrows 90,000 Total Investment $200,000	Immigrant cash $110,000 Immigrant borrows 90,000 Total Investment $200,000	Immigrant cash $110,000 Immigrant borrows 90,000 Total Investment $200,000
The intermediary provides $200,000 to the business for the preferred shares.	The intermediary provides $200,000 to the business for the preferred shares.	The intermediary provides $200,000 to the business for the preferred shares.
The business signs a promissory note for $130,000.	A shareholder of the business purchases an option on the preferred shares by paying the intermediary $125,000.	The business agrees to redeem the shares at the end of five years for $90,000 the same amount as the loan.
The business provides $100,000 payment on the note at closing.	The shares are assigned to the intermediary by the immigrant as security for the loan.	The business pays the $90,000 at the date of closing which is held on deposit by the intermediary until the five years are up.
The business pays the $30,000 to the intermediary over five years.	There are no dividends.	There are dividends allowed but will only be paid if declared, none are declared.
The shareholders of the business provide a personal guarantee or other security to cover the $30,000 commitment.	The shareholders of the business do not need to pledge additional security.	In some cases shareholders are required to pledge personal guarantees.
Results to Business: Business receives $75,000 on closing but pays out $30,000 over five years for net proceeds of $45,000. The net present value of receipts equal $55,000.	Results to Business: Business receives $55,000	Results to Business: Business receives $55,000
The intermediary receives from business on closing: Intermediary fees $25,000 Difference on loans 10,000 Loan Payment over five years 30,000 Total $65,000 Less agent fees, approximately (40,000) Net fees $25,000	The intermediary receives from the business on closing: Intermediary fees $20,000 Difference between the loan and the option 35,000 Total $55,000 Agent fees, approximately (40,000) Net fees $15,000	The intermediary receives from the business on closing: Intermediary fees $55,000 Agent fees, approximately (40,000) Net fees $15,000

3.97 The amount paid by the immigrant for the investment varied from $105,000 to $120,000 depending on the country of origin and the agent the immigrant uses. As part of the program requirements IIDI implemented a policy requiring the immigrant to certify that they had not been charged more than $120,000 for the investment. In

exchange for the services provided, the intermediary receives a fee which is built into the financing structure.

3.98 The role of the intermediary is an important function under the Program. IIDI required each business to use an approved intermediary. We looked for the process to approve intermediaries to be open and available to all interested, qualified parties.

3.99 The Program evolved over a number of years. We were advised that initially there was a communication to accountants and lawyers in Prince Edward Island inviting their participation in the program. A number of intermediaries became involved in the Program. When the volume of applications increased, IIDI required the immigrant files to be submitted in a standard format. IIDI's expectations for the intermediaries increased and we were advised that consideration was given to going to a request for proposals for intermediary services. Instead the list of approved intermediaries was frozen and no new intermediaries were approved after October 2006. We were advised interested parties that came forward after this date were declined.

3.100 To offset any potential liability that could arise as a result of their involvement with the PNP, intermediaries of record at October 2006 were required to maintain a security deposit of $300,000 with IIDI. We reviewed these documents which are held in the form of an irrevocable letter of credit accessible to IIDI. We found that for one intermediary the letter of credit expired in December 2007 and another is due to expire in March 2009. For one intermediary, a cheque of $300,000 was provided with a replacement letter of credit issued as of October 2008. We also noted that two of the seven Agreements indicate the funds could not be accessed without a court order whereas the other five indicate IIDI can access the funds as required on presentation of the original letter of credit. These letters of credit were put in place to provide security if IIDI needed to draw on them. Due care is required to ensure they are kept current.

3.101 In the early days of the Program there were no limits established on the amount of fees the intermediaries could charge. There were wide variations in the fees which meant the net

investment capital that was provided to the Island business varied as well. Some businesses received as little as $25,000 from each unit. We expected the amounts charged by the intermediaries to be consistent and where differences existed that they would be justifiable.

3.102 IIDI was aware of wide variations in the net amount of investment capital provided to the Island businesses. In October 2006, the Program was significantly revised. IIDI set a requirement that each investment had to provide at least $55,000 per unit to the business before legal and accounting fees and this was communicated to each intermediary. This requirement reduced the variations in the amount of money provided to the Island business as well as in the fees charged by the intermediary to the business.

3.103 Most intermediaries receive $55,000 from which they pay the agent located in the foreign country. The amounts charged by these agents vary depending on the country of origin, the relationship with the intermediary, and the volume of business. We were advised that the amount per file paid to the agent ranged from $30,000 to $45,000. One of the intermediaries interviewed has an exclusive arrangement with one agent and the majority of fees collected are provided to that agent, with the intermediary receiving a salary, commission and reimbursement of overhead.

3.104 In May 2008, IIDI obtained information from each of the intermediaries on how many immigrant files they had in process which had not been submitted to IIDI. At that time there were approximately 1,700 files in process which had to be completed and nominated by September 2, 2008 in order to fall under the requirements of the old regulations. IIDI determined that an additional 320 files was all that could be processed in the time frame and allocated this number of files to the intermediaries based on their historical percentage of files processed. IIDI had been advised by Treasury Board it would be required to provide a budget transfer to the Department of Education to offset the financial impacts of immigrant children in the school system. The amount was later determined at $4.2 million for the 2008-09 school year. The Deputy Minister approached five of the seven intermediaries and offered them an additional allocation of files

in exchange for an education contribution of $2,500 to $3,000 per file. This added an additional 210 files to the total files that had to be processed and resulted in additional revenue to IIDI of $550,000. One of the intermediaries we interviewed advised that in some cases these costs were passed on to the immigrants although it was IIDI's intention that these charges be paid out of the intermediary proceeds. We could find no formal authorization for this charge, and the allocation of additional files was not offered to all intermediaries.

3.105 The role of intermediary is critical to the success of the Provincial Nominee Program. With the volume of nominees processed in 2008 there was a potential for substantial business revenues for those intermediaries approved under the Program. There are currently a variety of financing structures, fee structures, and agent relationships in place. Intermediaries are businesses that operate at arms length to IIDI. As IIDI has the authority to control the number of approved intermediaries they deal with, it is imperative for transparency that there be criteria established around qualifications, experience, and operating expectations and that these be consistently applied for intermediaries to acquire and retain approved status under the Program.

Recommendations

3.106 Similar to a licensing procedure, IIDI should develop and apply criteria that intermediaries must meet in order to achieve and maintain approved intermediary status.

3.107 IIDI should ensure that letters of credit provided by intermediaries are up to date and consistently accessible.

Trust fund for Rejected Nominees

3.108 Terms and conditions are set out for the preferred share investments arranged by each intermediary. The term sheets of each intermediary contain a provision dealing with the potential outcome of a federally declined or withdrawn immigrant. Most of these term sheets discuss a replacement mechanism whereby any federally declined or withdrawn immigrant would be replaced by another

nominated investor resulting in his or her full investment proceeds being refunded. However, with the change to the regulations in September 2008, replacement investors are no longer an option.

3.109 In response to this issue IIDI sent a directive to intermediaries in April 2008 instructing them to withhold $5,000 per unit from the net proceeds available to businesses. These funds are held in trust and intermediaries are to draw down on their respective trust funds to refund any immigrants who are declined federally. The directive also instructed intermediaries that the interest earned on these trust accounts was to go first to pay for administering the trust funds, with the balance to be given back, on a pro rated basis, to the businesses that contributed to the fund. Once all of an intermediary's clients have either received their permanent resident visa or been declined federally, the intermediary is to disburse the remaining balance, on a pro rated basis, to the businesses that contributed to the fund. The directive does not outline a mechanism to regularly report on the activities and balances in these trust funds.

3.110 There were 1,812 immigrant nominations that were subject to this $5,000 hold back. Intermediaries confirmed in writing that the balance of their trust accounts at January 2009, excluding interest, totalled $9,005,000. The original balance had been $9,060,000, but there has already been one refund for $55,000. Given the remaining balance of $9,005,000, there are enough funds left to cover 163 rejected investors, working out to a rejection rate of approximately 7 percent based on the fact that 2,281 nominees have not received federal approval as of January 31, 2009.

3.111 Historically, PEI's rejection rate at the Federal level has been approximately 2 percent. However, this historical rate is not a reliable figure to use in projections of future refund rates because of two main factors. First, the bulk of immigrant applicants in 2008 (representing 42 percent of the entire population of immigrant investors over the life of the Program) did not have to travel to PEI for an interview since interviews were conducted overseas. As such, these people did not require a visitor visa, which typically acts as a screening process for applicants. Second, immigration agents have been promoting PEI's program because of its favorable processing times, but given the

volume of nominations in 2008, delays in processing at the federal level are anticipated. These delays may result in increased withdrawals by nominees. In a letter received October 2008 federal representatives expressed concern that even a 10 percent refund coverage might not be sufficient. A refund rate of 10 percent would require funds of approximately $12.5 million.

3.112 This potential liability is made more complicated by the fact that there is disagreement among key stakeholders regarding with whom the potential liability rests. There is no PNP policy that states a rejected investor or an investor who withdraws will be refunded his or her investment proceeds; rather, this is an arrangement between the intermediaries and the immigrant investors. There are differences in the wording of agreements among the intermediaries. For example, one intermediary's documents state they will not refund a withdrawal.

3.113 As indicated previously, $55,000 worth of funds may be drawn down from the rejected investor trust fund for refunds. However, immigrant nominees invested between $105,000 and $120,000, and as such, are due back a further $50,000 - $65,000. There is currently disagreement as to where the balance should come from. Some intermediaries we interviewed stated the liability rested with the intermediary while others indicated that they were not liable and noted other potential sources of funds such as: the business that received the investment, or a portion of the agent's commission as one half of the agent's commission is to be held in trust until the nominee has received federal approval. This potential liability would be between $11.4 million and $14.8 million at a 10 percent rejection rate.

3.114 In essence, there are two issues: who is responsible to come up with the remaining $50,000 - $65,000 for each refund and who is responsible for any potential shortfall in the rejected investors trust fund. IIDI is currently seeking legal advice on these matters. Even if there is no monetary liability to IIDI, there are potential impacts if rejected or withdrawn immigrant nominees are not able to recover their full investment.

Recommendations

3.115 IIDI should continue to seek legal advice on the potential liability related to investor refunds.

3.116 IIDI should implement a reporting framework with the intermediaries to include regular reporting of balances and activities of the rejected investor trust fund accounts.

Conflict of Interest

Members of the Legislative Assembly

3.117 The Conflict of Interest Act applies to all elected Members of the Legislature. Subsection 14(2) of that Act states:

> *No member shall have an interest in a partnership or in a private company that is a party to a contract with the Government of Prince Edward Island under which the partnership or company receives a benefit.*

Subsection 14(4) of the Conflict of Interest Act provides as follows:

> *"Subsection (2) does not apply if the Commissioner is of the opinion that the interest is unlikely to affect the member's performance of the member's duties."*

3.118 As part of our audit we determined that from the inception of the PNP four corporations were approved to receive units while the related Member was a shareholder and was elected to the Legislature. This does not include instances where shares are held in a blind trust or a family trust. Section 14(2) of the Act does not apply to these situations. For three of these companies the related Member had requested and received a letter of clearance under the Conflict of Interest Act from the Conflict of Interest Commissioner.

3.119 The Conflict of Interest Commissioner provided a letter of clearance to those MLAs who requested a ruling. In his ruling he stated that if the Member made an application under the Program he

would not be in breach of the Conflict of Interest Act. His rulings were based on the following premises:

- Once the business is deemed eligible IIDI's involvement ends;
- The intermediary and the immigrant select the business and ensure investment is made;
- There is no contract with government nor any involvement other than through IIDI;
- IIDI assesses business eligibility based on guidelines applicable to all businesses; and
- The intermediary is independent of government.

3.120 As a result of our audit we had some concerns about these premises. For example, the Use of Proceeds Agreement implemented in October 2007 is a contract that confers a benefit to the business involved. Under this Agreement the eligible business commits to IIDI to use the proceeds within two years in accordance with the approved business plan or could pay a penalty to IIDI of $55,000 per unit. Of the four corporations noted above, three entered into a contract with Government through the Use of Proceeds Agreement. The other corporation was approved prior to October 2007 did not sign a Use of Proceeds Agreement and did not request a letter of clearance from the Commissioner.

3.121 As an elected representative, each Member of the Legislature holds a public office. It is appropriate that each Member be held to a high standard in the conduct of his or her business affairs. The Conflict of Interest Act is important in protecting the integrity of the public office held by each Member.

3.122 Each Member who applied to the Conflict of Interest Commissioner clearly intended to avoid a conflict situation. The Provincial Nominee Program was complex and evolved throughout the period of review. For example, the introduction of specific required documents had an impact on how involvement in the Program was interpreted under the Conflict of Interest Act. In addition, certain sections of the Act are broad and open to interpretation. For example, the section on contracts with government does not address the

application of this section to family members or family trust arrangements.

Recommendation

3.123 The Legislative Assembly should review the Conflict of Interest Act to determine if revisions can be made to clarify conflict of interest situations for Members.

Deputy Ministers

3.124 Deputy Ministers are employees of government and as such are subject to the Conflict of Interest Guidelines under the Treasury Board Policy and Procedures Manual. Under Section 3(a) of the Guidelines it states:

> *Conflict of interest exists in any situation in which an employee either for himself/herself or some other person attempts to promote a private or personal interest which actually or apparently:*
>
> *(i) interferes with the objective exercise of the employee's duties in the civil service;*
>
> *(ii) is advanced or enhanced because of the employee's position with the government.*

3.125 We identified three Deputy Minister level employees and/or their spouses who received units under the Program while they were in their positions. In one case the Deputy Minister's involvement under the Program was subject to a review by senior bureaucrats. The report completed as a result of that review stated "while we could see no evidence of an actual conflict of interest as defined by the Conflict of Interest Guidelines, we could see where it could be seen to be an appearance of conflict..."

3.126 Under the Principles section of the Treasury Board guideline it states.

> *6(f) Employees shall not take advantage of or appear to take advantage of their official position....*

Given the position of authority at the Deputy Minister level there is an appearance that these individuals could have used their positions to gain approval under the Program and therefore were in a conflict based on the Treasury Board guidelines.

3.127 The Deputy Minister level is the highest level of authority within the management of government. The Conflict of Interest Guidelines are written in a broad manner to have application to all government employees. Those in higher positions of authority should be held to a higher standard and often those at the Deputy Minister level will have more exposure to potential conflict situations. In a number of other provinces there are more comprehensive Conflict of Interest provisions in place for employees at the Deputy Minister level.

Recommendation

3.128 The Treasury Board Conflict of Interest Guidelines should be clarified and strengthened regarding their specific application to and the expectations for Deputy Minister level employees.

IIDI Revenue

3.129 Revenues from the Provincial Nominee Program to IIDI include the following:

- processing fees from both the immigrant applicants and the business applicants;
- fees charged to intermediaries and agents in the form of a settlement and retention fee, education contribution, and interview fee;
- interest on the majority of the good faith and language deposits held; and
- defaulted good faith and language deposits.

3.130 Initially fees were introduced to offset the administrative costs of the Program. In the summer of 2008 a number of fees were introduced and others increased to offset projected settlement and education costs related to the increased nominations. This increase in revenue has been mainly responsible for the increase in funds

flowed through to the Province as a general source of revenue. **Exhibit 3.7** illustrates the revenue received by IIDI as a result of fees under the Provincial Nominee Program, the majority of which relate to the Immigrant Partner Category.

EXHIBIT 3.7
PNP REVENUE SOURCES
ALL CATEGORIES
($000)

	Audited 2006/07	Audited 2007/08	Unaudited Jan 31/09
Application Fee Revenue	$1,771	$3,449	$ 2,720
Business Fee Revenue	-	780	4,849
Settlement and Retention Fee	-	-	1,665
Education Contribution	-	-	549
Interview Fees	-	-	3,422
Interest Income	176	888	1,413
Total	**$1,947**	**$5,117**	**$14,618**

3.131 Immigrants pay a $2,500 processing fee to IIDI. In October 2007, IIDI introduced a business fee as well. Initially, the business fee ranged from $1,500 to $2,500 per unit, depending on the number of units received. At that time, a business receiving 4 investment units had to pay a $10,000 fee to IIDI. In July 2008, towards the end of the Program, IIDI raised its fees by $2,000 per unit; thus a business receiving 4 investment units had to pay an $18,000 fee to IIDI.

3.132 IIDI introduced three fees collected through intermediaries: a settlement and retention fee, an interview fee, and an education contribution. In May 2008, IIDI implemented a $1,000 settlement and retention fee. The fee was intended to be paid from the agent's commission, but some of the intermediaries we interviewed absorbed at least part of the cost to maintain good relations with their agents. This fee amounted to approximately $1.7 million to IIDI. In 2008, when interviews were held overseas in Hong Kong and Dubai, IIDI charged intermediaries a $2,500 interview fee for each nominee. This fee, amounting to $3.4 million, was charged to intermediaries directly and was based on the number of interviews performed for each

intermediary. These fees were passed on to the immigrants. Some of the intermediaries we interviewed charged an additional fee to the immigrant to cover their own costs for traveling overseas. The origin of the education contribution is discussed in another section of this report. This fee amounted to approximately $550,000 in total.

3.133 IIDI earns interest on the majority of the good faith and language deposits held. Prior to April 1, 2006 the deposits accrued interest to the immigrant investor; now, the interest accrues to IIDI.

3.134 When an immigrant does not come forward to claim his or her deposit and demonstrate that the terms and conditions for a refund have been met, the deposits are defaulted and taken into revenue by IIDI. Language deposits were first introduced in 2005-06, and as of March 31, 2008 only two language deposits were defaulted. This is a conservative approach.

3.135 We looked at a sample of defaulted deposits during calendar 2008 to ensure that documentation existed to support the default and that the transaction was properly authorized. Based on our testing of defaulted deposits, controls exist and are operating as intended to ensure that defaulted deposits are properly supported and authorized. **Exhibit 3.8** indicates amounts taken into revenue by IIDI.

EXHIBIT 3.8
ISLAND INVESTMENT DEVELOPMENT INC.
DEFAULTED DEPOSITS
($000)

	Audited 2006/07		Audited 2007/08		Unaudited Jan 31/09	
	#	$	#	$	#	$
Good Faith Deposits	89	$2,379	76	$2,057	36	$ 989
Language Deposit	0	0	2	41	8	160
Total	**89**	**$2,379**	**78**	**$2,098**	**44**	**$1,149**

3.136 Historically, IIDI has been conservative in its defaults of good faith deposits. It has recently introduced internal procedures to

streamline the process including reminder letters to immigrants that their one year anniversary is approaching. The resulting impact of potential defaults will not be realized by IIDI until several years into the future since the vast majority of the immigrant investors have made their deposits, but have not yet landed in Canada. In fact, assuming federal processing times are anywhere from two to three years plus the one year wait time under the terms of the agreements, the disposition of the deposits may not be known until fiscal 2012-13.

3.137 We questioned IIDI finance staff on their fiscal 2009 year-to-date defaults, and we were advised that they are making every effort to contact these immigrants to initiate the internal default processes. They fully expect that defaults will be addressed for the 2009 Financial Statements.

3.138 All of these additional revenues have had an impact on the funds that are flowed through to the Province's general revenues. In the last two fiscal years, IIDI transferred $2 million to the general revenues of government. For fiscal 2008-09, IIDI originally budgeted a transfer of $4.1 million; however, this budgeted transfer has been increased to $8.4 million in the third quarter estimates. This marks a substantial increase to the Province's general revenues. IIDI has also made a commitment to transfer $4.2 million to the Department of Education to help offset additional education costs related to immigration.

Recommendation

3.139 IIDI should review its deposits to ensure the defaulted revenue reported is complete.

Evaluation and Settlement Strategy

3.140 A key aspect of the Federal Provincial Cooperation Agreement on Immigration refers to an evaluation of the Program. We were informed that work has commenced on the development of an evaluation framework for all Provincial Nominee Programs. No joint evaluation projects have been completed as yet, although some

provinces have undertaken their own evaluation of the Nominee Program in their respective province.

3.141 The Immigrant Partner Category of the PNP has been in operation since 2001. Under this Category 3,422 immigrants have been nominated by the Province and significant economic development funds have been provided to Island businesses. We expected IIDI to have carried out an evaluation of the Program and an assessment of the extent to which the objectives of the Program have been achieved. We found an evaluation of the Program has not been completed.

3.142 An evaluation is important to ensure the Program is achieving its intended results and to make appropriate adjustments on a go forward basis. We expected that IIDI would provide information on the goals and results achieved by the PNP in an Annual Report to the Legislative Assembly as required by the Financial Administration Act.

3.143 We noted that IIDI does not provide an Annual Report to the Legislative Assembly. Information provided is limited to annual financial statements. The Program has an important impact on the Province's economy, Government services, and the population, and information on the PNP should be included in the Annual Report of IIDI.

3.144 The Federal Provincial Cooperation Agreement includes provisions for the establishment of a Joint Program Management Committee and the sharing of information between the Federal and Provincial levels. From our discussions at both the federal and provincial levels as well as review of minutes of meetings, we found that there was no joint program management committee. However, there is a Federal/Provincial/Territorial working group which meets bi-annually and provides reporting of nominations and targets for this Program.

3.145 Information obtained from IIDI indicates that 1,065 PEI nominees landed in Canada from the inception of the Program up to February 2009. Of these, 368 have registered with IIDI as having arrived on PEI. These numbers do not include spouses and

dependent children. Under the PNP each immigrant must clearly state his or her intention to reside in PEI. However, under the Charter of Rights and Freedoms, once an individual is issued a permanent resident visa they may reside anywhere in Canada. The documentation provided to the immigrants requests that they register with IIDI when they arrive on PEI. This does not always occur.

3.146 The Program has been in operation for a sufficient period of time to have some level of evaluation completed. However, we acknowledge that there is a time lag between the nominations and the arrival in Canada. Our interviews with immigrants who are on PEI indicate that at a minimum there is an expectation gap between what the immigrants expected and what the Program provided.

3.147 We interviewed a sample of immigrants who are now PEI residents. We wanted to obtain information on their experiences with the Program and give them an opportunity to express any concerns. We attempted to contact immigrants individually for interviews but had difficulty obtaining current contact information for most immigrants. We placed French and English advertisements in two local newspapers, posted a translated advertisement on an active Chinese website and invited Korean immigrants to come forward through the PEI Korean Association. It is important to note that the 2008 nominees would not yet be on PEI as the Federal processing of applications can take up to several years to complete. One of our interviewees did receive his nomination during 2008 and was on PEI under a visitor visa.

3.148 In our interviews with immigrants the following concerns were expressed:

- The immigrants were confused about the Program details, specifically when it came to the breakdown of where the investment money went.
- Immigrants were disappointed with their lack of involvement with the investee company. None of the immigrants we interviewed had had any contact with the investee company since making their preferred share investment. The immigrants we interviewed had

not received notice of Board meetings nor had any received financial statements or other reporting from the investee company.

- Immigrants were disappointed with the processes surrounding the good faith and language deposit refunds. Specifically, they felt that policies kept changing throughout the Program and that IIDI requested additional information to substantiate the requirements for the good faith deposit refund that was above what would reasonably be expected.
- Immigrants were disappointed with the lack of government support after coming to PEI with respect to finding employment and/or learning about investment opportunities.

Program Details and Breakdown of Costs

3.149 We expected IIDI, as the program administrator, to ensure key details were well communicated to the immigrant nominees. We noted that the interview process was not intended as an opportunity to fully explain the Program when the immigrants were interviewed during the assessment stage; rather, these interviews were used to gather additional documentation, clarify information, and assess the applicant's English skills. IIDI stated they always gave immigrants a chance to ask questions. IIDI informed us that there is an onus on the immigrant nominees to fully understand the Program details and where their investment funds would go. IIDI has stated on its website that the immigrant nominees should seek independent legal and accounting advice before making their investment. Intermediaries advised that they explained the process and the financing when meeting with the immigrants and that the agent was responsible for having documents translated.

Lack of Involvement With Investee company

3.150 The investee company signs an undertaking to the immigrant stating that it will give notice of Board of Director meetings and will provide annual financial statements and other reporting on statutory remittances. We were advised that part of the reason information was not received is because businesses did not have the proper contact information to send the immigrant such documents. Intermediaries told us that businesses would come to them with packages for the

immigrants. Some intermediaries would forward such information to the immigrant's agent, while others indicated that they would not provide such a service.

3.151 Intermediaries indicated to us that, from their dealings, immigrants' key focus was on obtaining a permanent resident visa and the investment details were secondary. Several intermediaries stated that not one immigrant has come to them looking for information on the company in which they invested.

3.152 We noted that in many cases, the immigrant had provided power of attorney to his or her intermediary meaning that most of the investment documentation was signed by the intermediary on behalf of the immigrant. Also, we noted that most of the investment documentation regarding the investee company was in English.

3.153 The Immigrant Partner Category of the PEI Provincial Nominee Program is currently suspended. Given the concerns expressed by immigrants and based on the fact that the large volume of nominations recently approved will translate into increased numbers of immigrants arriving in PEI over the coming years, it is an opportune time for Government to examine the successes and shortcomings of the Program. This information would help to increase the effectiveness of any new Immigrant Partner Program developed.

Recommendations

3.154 IIDI should conduct an evaluation of the Immigrant Partner Category of the Provincial Nominee Program.

3.155 In accordance with the Financial Administration Act, IIDI should provide an Annual Report to the Legislative Assembly which includes information on the PNP.

Settlement Strategies

3.156 The mandate of the Population Secretariat is to work towards an annual population growth of 1.5 percent. Under the Island Prosperity Strategy the Population Secretariat has been revitalized

and is in the process of developing new objectives and related activities in the areas of retention, repatriation, recruitment and settlement. The mandate of the Population Secretariat extends beyond the immigrants arriving under the PNP to all areas of retention and immigration. The Secretariat is initiating strategic collaboration among the various departments to improve access to services for the anticipated arrival of immigrants recently nominated under this Program.

3.157 While the Population Secretariat is developing programs to address immigration long term, we know from the nomination of 1,877 principal immigrants in the summer of 2008 that PEI can expect the arrival of a significant number of people over the next several years under this Program. It is important to remember that the Immigrant Partner Category sought out individuals with a significant net worth and management experience. However, our interviews indicated that the immigrants residing on PEI had difficulty obtaining various services and information on employment and investment opportunities. Where IDII is successful in terms of attracting these immigrants to come to PEI, services should be in place to help them integrate into the community and establish a permanent residence here.

3.158 The PEI Association for Newcomers (ANC) is a non-government organization that provides services to immigrants on PEI. This organization provides a number of different basic programs to assist individuals in obtaining services from government such as employment services, registration in schools, and access to health care. The ANC keeps a record of the number of individuals who have registered with them for services, their country of origin, and whether they arrived through the Provincial Nominee Program or other programs. The ANC has been collaborating with IIDI to assist them in improving information on actual numbers of immigrants resident on PEI as a result of the PNP. There are limits on what the Association can provide based on funding levels. There is a need for the newly revitalized Population Secretariat and the Newcomers Association to work together to ensure there is a comprehensive level and type of service provided without duplication.

Recommendation

3.159 The Province should develop a strategy to improve the settlement services available to immigrants.

MANAGEMENT RESPONSE

3.160 Our recommendations were discussed with senior officials of Island Investment Development Inc. and a written response will be provided.

4. IN-PROVINCE PHYSICIAN PAYMENTS

OVERALL COMMENTS

4.1 Remuneration to physicians represents approximately 16 percent of the budgeted expenditures of the Department of Health; as such, control over these expenditures impacts overall budgetary control.

4.2 In general, the Department has system controls and procedures in place to monitor the legitimacy and accuracy of payments. However, some weaknesses were noted during our audit in the areas of renewal of personal health numbers, deactivation of physician billing numbers and the internal audit strategy. In addition, the computerized system for processing physician claims requires stronger access controls and monitoring procedures to prevent and detect errors within the system, and to protect the confidentiality of patient information.

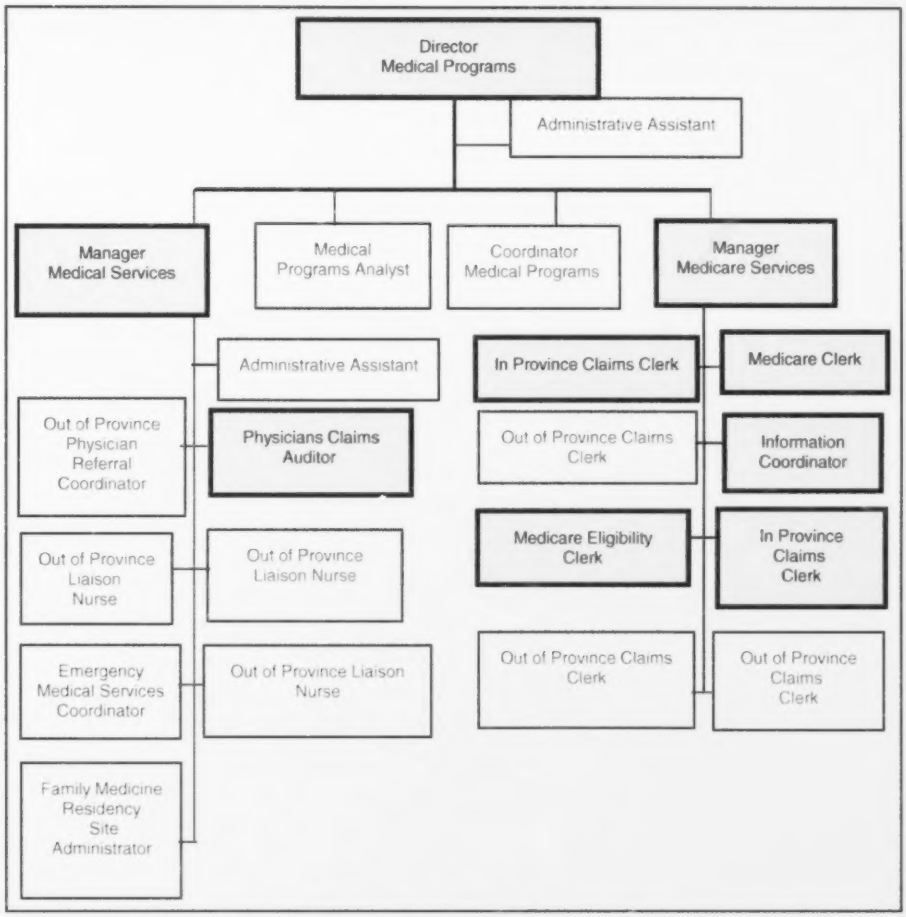
4.3 Cost comparisons of fee-for-service and alternate pay models for family physicians indicate that on average alternate pay models are more costly. Alternate pay models are offered to be competitive with other provinces in recruiting and retaining physicians. The management model in place in the Government operated Family Health Centres provides for monitoring of the productivity of salary and contract physicians while those in private clinics do not have the same oversight. In order to address efficiency and cost effectiveness the Department needs to improve controls to ensure hours and level of service are maintained.

BACKGROUND

4.4 In 2005-06 the Regional Health Authorities were dissolved and the administration of health services was brought under the authority of the Department of Health. The Department was reorganized into nine Divisions to administer health services. The Medical Programs Division of the Department of Health is responsible for the delivery of medical programs and services which includes managing payments for In-Province Physician Services.

4.5 **Exhibit 4.1** shows the key positions in the Division which have responsibilities related to In-Province Physician Payments.

EXHIBIT 4.1
DEPARTMENT OF HEALTH
MEDICAL PROGRAMS DIVISION

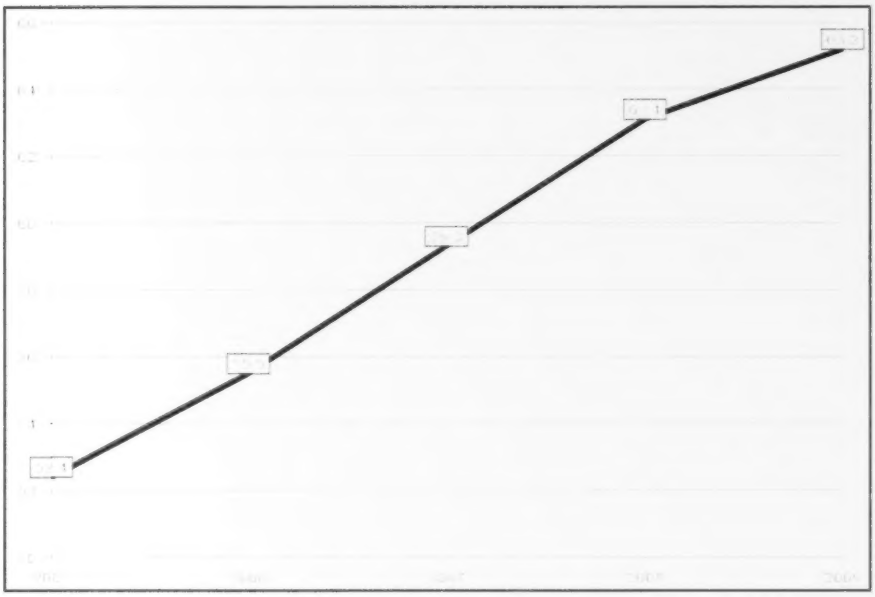


4.6 The IT Shared Services Branch of the Department of the Provincial Treasury is responsible for the provision of information technology services within Government.

4.7 The 2008-09 budget estimate for In-Province Physician Services is $65.2 million which represents 16 percent of the $398.4 million budgeted expenditures of the Department of Health. Since

2004-05 there has been an increase of $12.8 million or 24 percent in the budgeted expenditures for In-Province Physician Services. **Exhibit 4.2** shows the growth over this period. The main reason for this increase relates to the number of additional physicians. During the three years ended March 31, 2008 the number of physician positions filled increased by fifteen.

EXHIBIT 4.2
BUDGET ESTIMATES
IN-PROVINCE PHYSICIAN SERVICES
($Millions)



4.8 Payments to physicians have traditionally been made on a fee-for-service basis. Under this arrangement, physicians submit claims for each service they provide and are paid according to the tariffs for these services which are set in a collective agreement between the Medical Society of Prince Edward Island and Government. Government is responsible to pay the tariff to the physician and all costs associated with operating a practice such as rent, utilities, supplies, equipment and any office staff or other medical professionals employed in the practice are paid by the physician.

4.9 In recent years, the Department of Health has provided payment to physicians through alternate payment models. These alternate models can take various forms but generally the majority of the physician remuneration is in the form of salary or contract payments. The Department offers alternate payment packages to attract physicians to come to Prince Edward Island. Generally, recent physician graduates prefer an alternate payment model. Physicians that are paid through a salary or contract model are also entitled to receive fee-for-service payments for work they do outside of their regular hours of work such as during evening clinics.

4.10 **Exhibit 4.3** shows the breakdown of actual expenditures for In-Province Physician Services for 2007-08.

EXHIBIT 4.3
IN-PROVINCE PHYSICIAN PAYMENTS
EXPENDITURES
2007-08
($Millions)

Salary	$12.9
Contract	12.8
Fee-for-Service	31.6
Administration	2.6
Continuing Medical Education	.1
Insurance	.3
Other	2.5
Total	$62.8

4.11 Administrative costs for salary and contract physicians in private clinics were $2.6 million for 2007-08 and were paid out of the budget for in-province physician services in the Medical Programs Division. The administrative costs for family physicians in Government operated Family Health Centres were approximately $1.7 million in 2007-08. These costs were paid out of the Primary Care Division of the Department.

OBJECTIVES AND SCOPE

4.12 In accordance with Section 13 of the Audit Act, we conducted an examination of the management of payments for In-Province Physician Services provided through the Department of Health. Our audit focused on physicians' claims, payments to physicians, and the related system and procedures in place during the fiscal year beginning April 1, 2007 and ending March 31, 2008.

4.13 The objectives of our audit were to determine whether the system controls and procedures in place are sufficient to ensure legitimacy and accuracy of payments, to determine the efficiency and economy of alternate payment models for physicians, and to review the service contracts with the IT service provider related to definition of roles and responsibilities, and confidentiality and security of patient information. In conducting our audit we reviewed policies and procedures, tested samples of payments to physicians, interviewed numerous department staff and reviewed relevant files. Our audit did not include an assessment of the adequacy of the current physician complement approved for Prince Edward Island.

4.14 We performed our examination in accordance with the standards for assurance engagements encompassing value for money established by the Canadian Institute of Chartered Accountants and accordingly included such tests and other procedures as we considered necessary in the circumstances.

DETAILED AUDIT OBSERVATIONS

Physician Payments

4.15 Physicians on PEI have the option of being paid through several payment methods including fee-for-service, salary, contract and sessional. In addition, some physicians are entitled to receive a number of other stipends.

4.16 **Exhibit 4.4** shows the number of fee-for-service physicians compared to alternate pay physicians as at February 2007, March and December 2008. Although the number of practicing physicians

increased by 16.5 full time equivalent positions over this time period, the total number of physicians paid through the fee-for-service payment model declined. Of the 206.20 FTEs at December 2008, 85.85 are family physicians, 58 percent of which are paid through an alternate payment model.

EXHIBIT 4.4
BREAKDOWN OF FEE-FOR-SERVICE AND ALTERNATE PAY PHYSICIANS FULL TIME EQUIVALENTS

	December 2008	March 2008	February 2007
Fee-for-Service	76.00	79.50	80.80
Alternate Payment Plan			
- salary	89.25	79.35	76.95
- contract	25.95	25.45	18.45
- sessional	15.00	14.00	13.50
	130.20	118.80	108.90
Total	**206.20**	**198.30**	**189.70**

4.17 The Master Agreement is negotiated through a collective bargaining process between the Government of Prince Edward Island and the Medical Society of Prince Edward Island. The purpose of this Agreement is to establish a tariff of fees for fee-for-service as well as rates of pay for other methods of payment for health services. The Agreement sets out the rate of pay for over 1,000 different physician services covered by the Agreement.

4.18 The Medicare Office, located in Montague, is responsible for processing physician claims, administering physician payments, issuing physician billing numbers as well as registering those eligible for Medicare Services. There are nine staff members with the Medicare Office including a Manager, seven clerks who deal with claims, assessments and Medicare eligibility as well as one Information Coordinator.

Physician Billing Numbers

4.19 The Medicare Office issues billing numbers for physicians. A billing number must be used for a physician to submit claims for payment through the ICS.

4.20 We examined a sample of claims submitted by physicians paid by the Medicare Office for the fiscal year 2007-08. As part of our testing we reviewed the submitted claim to ensure that the physician who submitted the claim had an active billing number at the time the service was provided. Based on our testing, this control is working correctly as all of the claims in our sample were submitted with valid billing numbers.

4.21 We received several reports from the Department of Health which listed all physicians on PEI who had active billing numbers at specific periods of time. We noted that there were billing numbers listed on the reports for physicians who were no longer practicing on PEI, including cases where the physician was deceased. Physician billing numbers that remain active after the physician is no longer practicing on PEI increases the risk that invalid claims could be submitted and approved for payment by the Medicare Office. Discussions with the Medicare Office staff indicate there is no process in place within the Department to notify them on a regular basis of physicians who should have their billing number deactivated.

Recommendation

4.22 The Medical Programs Division should ensure deactivation of billing numbers is carried out on a timely basis.

Fee-For-Service Claims

4.23 Claims for services provided by physicians are submitted from the physicians' offices to the Integrated Claims System (ICS) via the internet through a secure network. Claims are validated by the system and processed through a rules engine which is built into the system. A claim is flagged for further assessment if it is rejected due to anomalies in the coding. Claims may be routed for further assessment

for a number of reasons. For example, claims submitted under new fee codes are flagged for a period of time.

4.24 We examined a sample of fee-for-service claims submitted to the ICS for payment. We expected to find that the claims submitted by the physicians were paid at the correct rates established in the Master Agreement for that service. For our sample items, all tariffs paid were in agreement with the Master Agreement in effect at the time the service was provided.

Salary

4.25 Salary is another payment option available to physicians. Salary physicians are paid through the Corporate Services Division of the Public Service Commission, are subject to the same controls, and receive similar benefits as other government employees. They are also provided with support from the Department for the administrative costs of their practice.

4.26 Salary levels are established as part of the Master Agreement. Physicians who are paid a salary receive a pre-determined amount pursuant to the Master Agreement based on whether they are family physicians or specialists. The Master Agreement also indicates that the normal hours of work shall be 37.5 hours per week to be provided between the hours of 8:00 a.m. and 8:00 p.m., Monday to Friday, unless otherwise agreed to between the physician and the Department. Salaried physicians are not permitted to bill fee-for-service during their normal hours of work and as a result any fee-for-service claims for salaried physicians are automatically flagged by the Integrated Claims System for manual assessment.

4.27 We selected a sample of salary physicians to determine whether payments were in accordance with the Master Agreement. No exceptions were noted. In addition, a sample of fee-for-service claims made by and paid to the salary physicians was tested to ensure that the claims were for medical services provided outside the salary physicians' normal salaried hours and that the tariffs paid agreed to the Master Agreement. Again, no exceptions were noted.

Contract

4.28 Another form of alternate pay available to PEI physicians is payment under a service contract. The difference between a contract and a salary physician is primarily that the contract physician does not receive all the employee benefits that are provided to a salary physician, however, the administrative costs are paid by the Province. Contract physicians are not permitted to bill fee-for-service during their contract hours of work and as a result all fee-for-service claims for contract physicians are to be automatically flagged by the ICS for manual assessment, similar to salary physicians.

4.29 We selected a sample of contract physicians to determine whether the contracts were paid in accordance with the Master Agreement. No exceptions were noted. In addition, a sample of fee-for- service claims made by and paid to the contract physicians was tested to ensure that the claims were for medical services provided outside the contract physicians' reported hours and that the tariffs paid agreed to the Master Agreement. Again, no exceptions were noted.

Sessional

4.30 Another form of remuneration paid to physicians for medical services is a sessional fee. These sessional fees are set out in the Master Agreement and are defined as a method of payment that is based on a time calculation or an hourly rate. Emergency room physicians based in PEI hospitals receive sessional fees for their services and bill using a generic personal health number. This process allows the Medicare Office to apply controls within the ICS to allow only the maximum daily Emergency Department hours per hospital as per the Master Agreement. For example, the Queen Elizabeth Hospital is funded for 48 hours of onsite coverage per day. If sessional fees exceed the allowed coverage, the hours on the last physician claim received by the system are rejected and manually assessed to determine validity.

4.31 Our audit sample included payments to sessional physicians. We examined payments to determine whether the amount paid to the

sessional physicians agreed to the hourly rate in the Master Agreement and that the number of hours claimed by the physicians agreed to the time sheets submitted by the respective hospital department. No exceptions were found.

Other Stipends

4.32 Physicians can also receive other amounts in addition to their salary, contract and/or fee-for-service payments for such things as administrative duties, long term care contracts and on-call payments. Additional administrative duties would include a physician taking on a role as a Chief of Staff of a hospital, a head of a hospital department such as Head of Surgery or a Medical Advisory Committee representative for their respective department. To be compensated for these roles, the Master Agreement has set out stipend amounts to be paid over the course of the year.

4.33 We examined a sample of stipends for long term care contracts and on-call retainers. For these stipends, we expected to find appropriate supporting documentation and payment in accordance with the Master Agreement. One physician in our sample was underpaid based on the stipend in the Master Agreement.

Recommendation

4.34 The Medicare Office should ensure that stipends paid agree to the rate approved in the Master Agreement.

Personal Health Numbers (PHNs)

4.35 Federal and Provincial legislation provide for coverage of basic hospital and medical treatment for eligible PEI residents. Residents who are registered and are eligible for medical coverage through Medicare are issued a Personal Health Number (PHN) which is identified on their health cards and is unique to each person. To become eligible for services, the resident has to submit an application to the Medicare Office and meet all eligibility requirements.

4.36 It is the practice of the Department of Health to renew PHNs once every five years. Generally, anyone who has been registered and is ordinarily resident in PEI is considered eligible to receive insured benefits. To maintain eligibility you must be present in the Province at least six months plus a day in each year.

4.37 We expected that the renewal forms for PHNs would explain the eligibility requirements to receive medical coverage in PEI and that those renewing would have to certify that they continue to meet the eligibility requirements. Upon review of these renewal forms it was determined that the eligibility requirements are not documented on the renewal form and the person does not have to certify that they meet the eligibility criteria. This poses a risk that ineligible people may be provided with insured services.

4.38 We expected that the Department would perform analysis on the PHNs to try to identify ineligible individuals and ensure payments were made only for services rendered to eligible PEI residents. We were advised that staff at the Medicare Office do some general analysis on the PHNs. We were informed that the number of PHNs is always higher than the population of the Province due to the timing differences of normal migration. Based on our analysis, we noted the number of active PHNs exceeds the population of PEI by approximately 7.5 percent or over 10,000 people. While we appreciate the amount of work involved in trying to reconcile these two figures, this is considered a significant difference. This difference should be reviewed as a risk exists that there are ineligible persons receiving insured services.

Recommendations

4.39 The renewal forms for a PEI Health Card should state the basic criteria a person must meet to be eligible for Medicare coverage on PEI and applicants should be required to confirm that they meet these criteria during renewal.

4.40 The Department of Health should review the current variance between the number of active PHNs and the population and take appropriate action where possible.

Management of Alternate Payments

4.41 The Canada Health Act Annual Report 2006-07 indicates that across Canada alternate payment plans seem to be the preference for recent graduates. These alternate payment plans have been made available to bring more physicians to the Province given most provinces in Canada offer varying forms of such payment arrangements. The traditional fee-for-service method is volume driven since the physician's compensation is tied directly to the number of patients served. Under the alternate payment model physicians often work less hours and see fewer patients. This causes issues for the Department of Health in controlling costs and ensuring productivity levels are acceptable.

4.42 We expected the Department to monitor the cost of alternate payment models and to carry out comparisons to the fee-for-service model. We were provided with a calculation prepared by the Department which indicates that based on 5,000 annual patient visits, salary and contract models for family physicians are more costly for the Department. Cost comparisons involve a number of variables and assumptions which impact the results of the calculation. The Department has recognized the need to focus attention on monitoring the productivity of the increasing numbers of alternate pay physicians. This monitoring entails such things as ensuring accurate shadow billings, which are claims submitted by alternate payment physicians to reflect what they would submit if they were fee-for-service physicians. Other procedures would include establishing benchmarks for physicians and introducing a reporting structure whereby physicians must be administratively accountable to a manager.

4.43 Prior to the current Master Agreement which covers the fiscal years beginning April 1, 2007 and ending March 31, 2010 alternate pay physicians were required to submit shadow billings on the medical services provided during their salary, contract or sessional hours of work. The claims do not generate a payment to the physician, but are an important source of information on services provided and productivity achieved.

4.44 As part of our work, we attempted to use this shadow billing information to compare the costs and productivity of a fee-for-service model to an alternate payment model. We were advised that the information on shadow billings was not complete because shadow billings were not always submitted by physicians. Further, shadow billing codes did not exist for some activities such as required hospital rounds, participation on medical committees, and paperwork that is required of a physician during his or her paid hours of work. It was therefore difficult to make a fair comparison on the productivity and cost of these alternate pay physicians. Under the new Master Agreement billing codes were added to capture work performed by the physician that is over and above patient time. The Department has also agreed to an incentive built into the new Master Agreement whereby the physician receives a bonus based on a percentage of his or her approved shadow billings. This incentive will improve the completeness and accuracy of the information provided by shadow billings and will provide important information to the Department to assist in monitoring the cost and productivity of physicians under various payment options.

4.45 The Department has also established productivity benchmarks for alternate pay family physicians. The average patient caseload per family physician should be between 1,200 and 1,500 patients with the goal of 20 to 23 patients per day during office hours. These numbers take into account the average time required for the physician to do other job duties, including hospital rounds.

4.46 The key to making the above effective, however, is to have a management structure in place to ensure that productivity levels are being monitored and productivity issues are being followed up on a regular basis. We found that Government operated Family Health Centres (FHCs) have managers in place whose duties include, among other things, supervising the physicians within their centres. This includes regular monitoring of patient caseloads and daily patient bookings, as well as communicating with and assisting physicians in improving their productivity if a problem is noted.

4.47 Family physicians in private clinics do not have a management structure and ongoing monitoring of productivity; however, they do

have access to physician advisors who provide guidance on clinical issues and some administrative issues where concerns are brought to their attention for follow up. The Department has received approval to develop a position of Manager of Alternate Payments. If this position is filled, administrative control for salary and contract physicians should be improved.

Recommendations

4.48 The Department of Health should use the information obtained from shadow billings to compare the costs and productivity of physician services under the various payment models.

4.49 The Department of Health should ensure adequate monitoring of the hours worked and the level of productivity of salary and contract physicians especially those in private clinics.

Internal Audit Function

4.50 The Department of Health is given the authority to audit and review claims by physicians through the Health Services Payment Act Regulations. The Master Agreement refers to the audit process as defined in the Health Services Payment Act and Regulations which charges the Department of Health with the responsibility to ensure accountability for expenditures on basic health services.

4.51 To perform the internal audit function the Department employs a Physician Claims Auditor. The auditor reports directly to the Manager of Medical Services. There is also a Medical Consultant who spends four days per month working with the Department. The Medical Consultant has several duties and works closely with the auditor helping to deal with questionable claims and appeals. It is the auditor's responsibility to conduct audits on fee-for-service payments to physicians and to provide an on-site resource for assessment staff located at the Medicare Office in Montague.

4.52 We expected that the internal audit function would include sufficient appropriate audit procedures to assess the accuracy and

validity of physician claims. The ICS generates a random sample of 200 claims every six week period. We expected that there would be a well defined set of audit procedures applied to each sample item and documentation maintained on the procedures performed and the results obtained. We noted that claims for services provided at hospitals, for example, are verified to the actual x-ray or other test procedures but services provided at physicians' offices are not always checked to documentation to verify that the service was actually performed. These types of services are estimated to account for 25 percent of the claims in the audit sample. Verification on a test basis of claims is an important procedure to substantiate that claims were legitimate and the service was rendered. By excluding services performed at physicians' offices, the audit coverage is limited and the usefulness of the audit process is affected.

4.53 We acknowledge that any effective internal audit function should consider the cost benefit of the audit procedures carried out. However, it is important that appropriate audit coverage is maintained and that claims from every physician are included in the audit testing.

4.54 We expected that regular reports would be provided to management to summarize the audit work performed. Such reports would state the physicians who were reviewed during each audit cycle, the number of claims reviewed in total and per physician, and the dollar value of such claims. They would also indicate which claims had adjustments identified. These reports would be provided for each audit cycle, as well as an annual report that summarizes the procedures and results of all audit cycles during the fiscal year.

4.55 For each physician who is included in the internal audit sample, a one page document is generated stating the physician's name, the claim number, as well as the service and patient details. This document is used to record the work performed by the internal auditor. An Annual Report stating the total dollars recovered during a fiscal year through the audit process is completed by the auditor and provided to the Manager of Medical Programs, the Director of Medical Programs as well as the Medical Consultant. This annual report is limited to the annual amount of recoveries for each year since 1996.

It does not include information on the number of physicians reviewed, the number of claims reviewed or any problems encountered.

4.56 The Physician Claims Auditor is also responsible for performing additional audit work on specific physicians. These types of audits are generally performed when the auditor identifies a potential problem with a certain physician's claims. They are not carried out on a regular basis. The auditor would visit the physician's office and review a large number of the physician's claims to determine if an issue exists. At the time of our audit it had been almost two years since one of these audits had been completed.

4.57 We expected that physicians' claims would be analyzed on a regular basis for anomalies, such as frequent claims for unusual services or unusual volumes of claims in a specific period. As mentioned previously, the Physicians Claims Auditor identifies issues but this is currently accomplished through the normal procedures on a sample of claims. Specific analysis should be carried out to identify unusual items that warrant further follow up.

4.58 We were advised that the Department is seeking funding approval for an additional auditor position. The intention is to develop, maintain and initiate a more comprehensive risk based audit program for all payments resulting from the Master Agreement.

Recommendations

4.59 Department management should ensure that internal audit procedures provide adequate coverage of fee-for-service claims from all physicians.

4.60 Periodic summary reports should be prepared and presented to management indicating the scope and results of the internal audit work completed.

4.61 The internal audit function should include analytical procedures to identify unusual patterns in physician claims. Any anomalies identified should be investigated and sufficient, appropriate audit evidence should be gathered to explain and document the issue.

Integrated Claims System

4.62 The Integrated Claims System, or ICS, is used by the Medicare Office to process claims for payment to physicians and to obtain information on medical services provided by salary and contract physicians in the form of shadow billings. The system is used by the Department of Health, however, the IT Shared Services Branch (ITSS) of Provincial Treasury manages the Service Level Agreement with the developer of ICS, the service provider. In this role, ITSS acts as the intermediary between the Department of Health and the service provider. Any problems encountered by the Department of Health with the application are first filtered through the IT specialists within ITSS and then, as necessary, to the service provider helpdesk for assistance. In addition, the service provider has a schedule of other service requirements outlined in the Service Level Agreement (SLA).

4.63 A Service Level Agreement was developed for the ICS to cover the period April 1, 2007 to March 31, 2010. However, as of January 30, 2009 this SLA was not signed. We were informed by ITSS that the services are being provided by the external party as laid out in the service agreement which includes monthly meetings and reporting.

4.64 The cost of services provided under the SLA is in excess of $100,000. As such, we expected that the SLA would have been presented to Treasury Board for approval. Section 13 of the Treasury Board Manual, Professional Services Contracts, Conditional Grants and Funding Agreements requires that all contracts and agreements in excess of $100,000 be approved by Treasury Board prior to the funds being disbursed by the Minister or Deputy Head. The SLA for the Integrated Claims System was not approved by Treasury Board.

4.65 The SLA does not meet all the basic service contract elements as presented in the Treasury Board Policy Manual, Elements of Professional Services Contracts. Most notably excluded from the SLA is an Indemnification and Assumption of Liability clause. Such a clause is intended to provide protection to government in the event a lawsuit arises related to something for which the service provider is responsible. Proof of insurance should also be requested under this clause in the agreement to ensure that the service provider has adequate coverage to protect government in the event of a lawsuit.

Recommendations

4.66 Arrangements with the external service provider for the Integrated Claims System should be formalized in a signed agreement and approved by Treasury Board as required by Treasury Board policy.

4.67 ITSS and the Department of Health should consult with the Risk Management and Insurance Section of the Department of the Provincial Treasury to determine the appropriate insurance coverage to be included in the Service Level Agreement for the Integrated Claims System.

4.68 Generally, we expected that the contractual agreement with the service level provider would address at least the following:

- The nature of the information which is accessible;
- Limitations on the systems employees can access;
- Security requirements for communications equipment;
- Responsibility for the protection of data;
- Screening requirements for employees;
- Training of employees in government security policies; and
- Accessibility to information for audit purposes.

4.69 In this case, the SLA does include a Non-Disclosure Agreement that addresses the nature of the information that is accessible. It outlines that the information that is disclosed to the provider and its employees is of "strictest confidence" and addresses the responsibility that the provider has for the protection of the data.

We were informed by ITSS that various access controls are in place within the provider's establishment.

4.70 The SLA and Non-Disclosure Agreement does not specifically address the security requirements for the communications equipment, the screening requirements for employees, the requirement for the training of employees in government security policies, or the accessibility of information for audit purposes.

4.71 A Government Information Security Policy has been drafted and would address these concerns, however, it has not been formally approved by the Information Technology Governance Council.

Recommendation

4.72 The Information Technology Governance Council should formalize a Government Information Security Policy. ITSS in coordination with the Department of Health should apply the approved policy requirements to the Service Level Agreement for the Integrated Claims System.

4.73 The information contained in the Integrated Claims System includes the payment information, addresses and personal information of PEI physicians, as well as, the personal health information of Prince Edward Island residents. This information is private and confidential in nature and should be strongly controlled and protected to ensure that breaches of this confidentiality do not occur. We expected to see strong access controls imposed at the Medicare Office. We found that access to the ICS does not require a separate user name and password. Access to ICS and the Health Network are synchronized. For each user who has ICS on his or her computer, when login to the Health Network is completed, access is automatic to the ICS. Single sign-ins pose greater risk for compromise of confidential information. Given the sensitivity and privacy of the information that is available on the Integrated Claims System, single sign on access is not sufficient and other options such as dual sign in and encryption should be implemented.

Recommendation

4.74 ITSS in coordination with the Department of Health should ensure additional access controls are implemented to minimize the risk of unauthorized access to confidential information in the Integrated Claims System.

4.75 Within the ICS, users performing similar duties can be assigned to groups and an access level for that group is determined. Access Level 1 provides the user with a view only access within the system operation assigned. Level 2 access gives the user the ability to view and to make changes to the data and various tables within the system operations they are assigned. In general, users should not be assigned access levels beyond what is needed to perform their duties.

4.76 The staff of the Medicare Office generally work in the following assigned areas: activation of PHNs, activation of new physicians, in-province claims assessment, out-of-province claims assessment, report generation, and internal audit. Some of the functions under these different areas are incompatible. For example, a user that can activate a new physician billing code should not also have the ability to adjust and process claims for that new billing code.

4.77 We reviewed the listing of user IDs and access levels provided by ITSS. We found that all staff at the Medicare Office have Level 2 access to all the same operations. This means all staff can create for example, a new provider in the system and adjust and approve claims. The degree of access is not adjusted for the different duties performed by each of these staff.

4.78 The rules function of the system that controls the way in which claims submitted are adjudicated cannot be easily altered. These types of programs changes must be made by IT personnel at ITSS or by the service provider.

Recommendation

4.79 ITSS in coordination with the Department of Health should ensure that:

- **only employees who require access to modify tables within the ICS have that access; and**
- **user access is limited based on requirements of the position.**

4.80 The system records the individual who last updated a table within the system. We expected to find that the system capability was utilized to monitor the access and changes made to ICS by government employees as well as the employees of the service level provider. According to ITSS and the Medicare Office no one is formally assigned to do this monitoring. There is a report that can be generated that indicates what was modified in the system by a user, however, it is only produced if a problem or concern is brought to their attention. The report itself is limited in that the parameters upon which this report is generated does not provide enough information. It shows only what records were accessed by the user, not what was modified.

4.81 The employees of the external service provider also access this personal information on a daily basis as part of their service agreement with ITSS. We expected to find that the external party access was regularly monitored. However, at the time of our audit the service provider was using only two generic user names and passwords to access the application. Users could not be easily identified. During the course of our audit, ITSS indicated it had taken action to assign unique user names and passwords to each employee of the service provider.

Recommendations

4.82 ITSS in coordination with the Department of Health should monitor the activity of users in the Integrated Claims System.

4.83 ITSS in coordination with the Department of Health should take the necessary steps to improve the usefulness of the monitoring report.

4.84 ITSS in coordination with the Department of Health should ensure that each employee of the service level provider requiring access to the Integrated Claims System has a unique user name and password to enable more accurate monitoring of activity.

Backup/Disaster Recovery

4.85 We expected to find that regular backup procedures existed for data contained in the Integrated Claims System. Data from the system servers is backed up daily and stored in a different area than the servers. Six months of backup is maintained at any given time. Removable drives on the database server are used to provide a quick recovery.

4.86 We also expected to find a documented plan for the recovery of the Integrated Claims System in the event of a disaster. Such a plan would assign responsibility and indicate the planned timelines for resumption of IT services. We found there is no disaster recovery plan in place for the Integrated Claims system.

Recommendation

4.87 ITSS in coordination with the Department of Health should develop a disaster recovery plan for the Integrated Claims System.

MANAGEMENT RESPONSE

4.88 Our recommendations were discussed with management and a written response will be provided.

5. DEPARTMENT OF SOCIAL SERVICES AND SENIORS GRANTS TO NON-GOVERNMENT ORGANIZATIONS

OVERALL COMMENTS

5.1 The Department of Social Services and Seniors does not have an overall strategy which documents the objectives and criteria for providing funding to NGOs. In addition, improvements are required in the documentation and approval of funding for NGOs. The Department recognized the importance of an accountability framework for grants provided to NGOs and took steps to put such a framework in place to hold NGOs accountable for the funds received from the Department. As of the fiscal year 2007-08, the Department started to require standard contracts to be in place to clarify the responsibilities of each party. However, based on our audit, there are weaknesses in the existing framework that need to be improved. Agreements were not in place for all NGOs funded by the Department in 2007-08. For those agreements that were in place, some provisions of the agreement were not being complied with and the Department did not actively follow up with NGOs to obtain required information, such as annual summary data on the clients served by the organization. As a result, it is difficult for the Department to assess whether funding objectives are being achieved.

BACKGROUND

5.2 The Department of Social Services and Seniors delivers a broad range of programs and services to the public. In some cases the Department provides funding to non-government organizations to provide public programs and services. Non-government organizations, (NGOs) are entities that are institutionally separate from government and business and operate with a "not-for-profit" philosophy. The essential aim of an NGO is to provide services and programs that are of public benefit.

5.3 Government supports a number of these organizations through the provision of operating grants, which in many cases, are the primary revenue source of the receiving NGO. The Department of Social Services and Seniors provides nearly $8 million annually to NGOs through three divisions: Social Programs, Child and Family

Services and Corporate and Financial Services. **Exhibit 5.1** provides a breakdown of the grants to NGOs.

EXHIBIT 5.1
DEPARTMENT OF SOCIAL SERVICES AND SENIORS
GRANT EXPENDITURES TO NGOs

Type of NGO	Expenditure 2007-08	Number of Organizations
Residential and/or Training Services for Intellectually Challenged	$4,889,600	8
Family Violence Support and Education Programs	839,400	2
Programs for Individuals with Physical and/or Intellectual Challenges	521,400	8
Seniors Programs	72,700	4
Support Programs for Island Families and Youth	1,444,400	13
Community Programs	57,300	2
	$7,824,800	37

5.4 The Department has categorized the NGOs it funds into three tiers as follows:

- Tier 1 NGOs provide services that are considered essential. If the NGOs in Tier 1 did not exist, government would be required to provide the service.
- Tier 2 NGOs provide services that are necessary, but not absolutely essential. If the services provided by Tier 2 NGOs were not delivered, pressure would be placed on caregivers and service providers in Tier 1, as well as government programs to replace the service.
- Tier 3 NGOs provide important, but not essential services for vulnerable population groups and organizations.

5.5 Prior to 2005, the majority of grants provided to NGOs that now fall under the Department of Social Services and Seniors were under

the management of the five Regional Health Authorities (RHAs) depending on the location of the respective NGO. When the regions were dissolved and the Department became directly responsible for these NGOs, it became evident there were variations in terms of funding, accountability, and reporting requirements. In an effort to standardize the process for administering these grants, the Department developed a standard service contract.

OBJECTIVES AND SCOPE

5.6 In accordance with Section 13 of the Audit Act, we conducted a value-for-money audit of the grants to non-government organizations through the Department of Social Services and Seniors.

5.7 Our audit focused on grants to non-government organizations during the fiscal year ending March 31, 2008.

5.8 The objectives of our audit were as follows:

- to assess whether the level of funding to specific non-government organizations was approved and supported; and
- to assess the systems and controls in place to determine whether organizations receiving grants and assistance used the funds to address the goals, priorities and legislative requirements of the Department.

5.9 We interviewed management within the Department of Social Services and Seniors who are responsible for planning, providing, and monitoring grants to NGOs. Our audit focused on NGOs that received payments greater than $100,000 in 2007-08. We examined numerous documents and financial reports related to these NGOs.

5.10 Our examination was conducted in accordance with standards for assurance engagements encompassing value-for-money, established by the Canadian Institute of Chartered Accountants and accordingly included such tests and procedures as we considered necessary in the circumstances.

DETAILED AUDIT OBSERVATIONS

Departmental Strategy

5.11 The Department's overall mandate is to support children, individuals, families and seniors to achieve their fullest potential. It works to fulfil its mandate through a combination of direct government programs, contracts with the private sector and the provision of operating grants to non-government organizations. There are a wide variety of programs and services provided by the Department. We expected the Department to have a documented strategy in place on funding for NGOs. Such a strategy should identify what types of organizations the Department will fund based upon which fit best with the Department's overall priorities. Such a strategy or policy statement would assist the Department in responding to the numerous requests for assistance received from organizations in the community.

5.12 We found the Department does not have an overall documented policy in place related to funding NGOs. The Department typically funds organizations that have historically received funding. As a result, the grants that are provided are annual amounts to cover operating costs with nominal increases based on increased costs or increased demands for service. A formal assessment has not been carried out to examine where available funds would be best used to address the priorities of the Department. Criteria have not been established to assess the eligibility of a NGO to receive grant monies from the Department and to enable the Department to evaluate which NGOs should receive funding. By not having established criteria to evaluate and compare all submissions, it is difficult for the Department to demonstrate objectivity when other interest groups come forward seeking funding from the Province.

Recommendation

5.13 The Department of Social Services and Seniors should develop a strategy outlining its objectives and criteria for providing funding to Non-Government Organizations.

Grant Approvals

5.14 We expected the Department to have an effective grant approval process in which all requests for funding are assessed against established criteria and management decisions on funding types and levels are well documented and supported. This would help to demonstrate objectivity in the approval process and aid in future decision making. In addition, we looked for controls to be in place over the payment process so that only approved organizations receive the grants. This would include authorization at appropriate levels for contract agreements, as well as for quarterly disbursements.

5.15 Budget submissions for NGOs are required to be received by October 31 for the next fiscal year and the funded NGOs are notified that the submissions are due. However, no standardized format exists for these submissions to ensure consistent and relevant information is provided to the Department by the NGOs.

5.16 The budget submissions we examined were in varying formats and provided different levels of information. The submissions varied from a few lines to a detailed line by line comparison to previous budget and actual expenditures. It was noted that these submissions were the primary evidence upon which funding decisions were made and there was no documentation in the files to show what, if any, analysis was performed on these submissions by Department staff. There was one NGO submission, for example, that showed a forecasted decline in external revenue of over $200,000 for 2006-07 and 2007-08 in comparison to the audited revenue amount reported in the organization's March 31, 2006 financial statements. There were no audited financial statements obtained for the March 31, 2007 fiscal year. Management in the Department could not provide an explanation for this difference or what steps were taken by

Department staff to follow up. In addition, this NGO received a 15 percent funding increase with minimal documented analysis by the Department.

Recommendations

5.17 A standardized format should be developed for budget submissions from NGOs.

5.18 Department staff should document the assessment of NGO budget submissions.

5.19 After budget submissions from the NGOs are reviewed, the Department compiles all the NGO requests for funding for the upcoming fiscal year. In most cases, the recommended amount presented to Treasury Board is different from the amount requested by the NGO. There was no documentation available to support the Department's adjustments to amounts requested for any of the NGO files we examined.

5.20 For 2007-08, the Department requested an increase to its NGO grant budget of $934,100; a $620,000 increase was received or $314,100 less than requested. The Department then allocated the actual funding approved to each NGO. In each of the NGO files we examined, there were copies of letters to the NGO that formally announced the budget allocation for 2007-08; however, there was no documentation in the file to support or reconcile how the final funding amounts were decided upon. In fact, in 15 of the 16 NGO files we examined, there was inadequate documentation to support the final decisions on funding levels.

5.21 For example, in one case an NGO received an increase in its core funding of $50,000 even though the submission from the Department recommended to Treasury Board that the organization not receive any increases for 2007-08. There is nothing in the file to support or explain why the Department changed its decision.

Recommendation

5.22 The Department should ensure that funding decisions for NGOs are well documented and supported.

5.23 Of the 16 NGO files we examined, 15 of them received operational grants from the Department in excess of $100,000 for the fiscal year 2007-08. Section 13 of the Treasury Board Manual, Professional Services Contracts, Conditional Grants and Funding Agreements, requires that all contracts and agreements in excess of $100,000 be approved by Treasury Board prior to the funds being disbursed by the Minister or Deputy Head. There were three NGOs that were in receipt of operational grants in the amounts of $214,000; $513,800; and $792,000 respectively where approval was not appropriately obtained from Treasury Board.

5.24 The Department pays the operational grants to NGOs in equal quarterly installments. All the quarterly payments made to the 16 NGOs in our sample were approved by authorized staff within the Department of Social Services and Seniors.

Recommendation

5.25 Funding agreements for NGOs in excess of $100,000 should be approved by Treasury Board as required by Treasury Board policy.

Agreements with NGOs

5.26 A signed contract or agreement clarifies and improves the relationship between the two parties involved and helps to achieve greater accountability. Without a signed agreement to identify performance expectations of each of the parties involved, it is difficult to determine if the expected results were achieved with the funding provided. The Department has developed a standard format contract for funding provided to NGOs.

5.27 There were 4 NGOs, out of 16 examined, where a signed agreement did not exist for the core operational funding provided for the 2007-08 fiscal year. The total value of grants disbursed in our sample without a signed agreement was just over $1.6 million. According to Department staff, contracts were not signed for these NGOs because restructuring in the form of governance and/or programming was occurring within these organizations. However, significant operational funding was provided to these organizations throughout this restructuring period. An agreement, therefore, should have been signed to ensure the expectations for the use of the grant funding were clearly understood by both parties, and accountability for this funding was maintained.

5.28 There were four instances in our sample where one-time grant payments, to cover such things as restructuring costs, were made without a signed agreement. The total of these one-time grants in 2007-08 was approximately $119,000. Without a signed agreement, the NGO is not obligated to formally report on the use of funds and results achieved.

Recommendation

5.29 For all funding provided to NGOs, the Department should ensure that signed agreements exist which clarify the performance expectations of the parties involved.

5.30 For the NGO files that did have signed contracts, there were several examples of non-compliance with the agreement on items that were required to be received by the Department before any grant money was disbursed. A certificate of good standing from Workers Compensation Board was to be obtained from each organization that signed an agreement. Of the 12 NGOs in our sample that had a signed agreement, the certificate was obtained for all but one, however, in all cases the certificates expired before the contracts were actually signed.

5.31 The standard contracts for the NGOs included an indemnification clause that require the NGO to obtain a minimum amount of insurance coverage, have the Government of PEI listed as an additional insured, and provide a certified copy of the insurance. In 4 instances out of 16, the Department did not obtain proof of insurance, 3 of which were organizations that did not have a signed contract. In 6 of the 16 NGOs examined, the NGOs did not have the Province listed as an additional insured on their policy. The Department did not obtain a certified copy of the insurance for any of the NGOs in our sample.

5.32 We found inconsistencies in the insurance policies of the NGOs funded regarding insurance coverage for instances of abuse. In one case, the insurance of the NGO specifically excluded abuse from the personal and bodily injury coverage of the policy. In other cases, abuse was insured with an established limit of liability, and in some cases it was not specifically mentioned. This is a significant risk since, in many of the NGOs we examined, the government is providing more then 90 percent of the operating funds for the organization.

Recommendations

5.33 The Department should ensure that required documentation regarding Workers Compensation and insurance coverage is current and received prior to payments being issued to the NGOs.

5.34 In coordination with the Risk Management and Insurance Section of the Department of the Provincial Treasury, the Department should review the insurance policies of the NGOs.

Performance Reporting From NGOs

5.35 As part of the standard agreement, within 90 days of the NGO's year end the organization is to provide the Department with an annual report which includes audited financial statements as well as information on clients served, staff, and the Board of Directors. In

most cases, 90 days translates into June 30. This information is important for the Department to gather on a timely basis in order to assess results achieved in relation to the funding agreement and to assist in making future funding decisions.

5.36 We expected that this information would be received on a timely basis as required by the funding agreements and where necessary, follow-up action would be taken by the Department to obtain the information for consideration in subsequent funding decisions.

5.37 As of September 8, 2008, 9 of 16 NGOs had not submitted their audited financial statements for the year ended March 31, 2008, and 9 of 16 had not submitted their annual report for the same fiscal period. Two of the NGOs that did not submit their audited financial statements or annual report for 2007-08 did not have a signed agreement.

5.38 In 10 of the 16 NGO files we examined there was no information on the number and type of clients served by the organization. Where the information was provided it was not in the detail that was required in the contracts. The contracts requested reporting on clients by such things as age, gender, level of care, number, re-admissions, discharges, number per geographic location, number with case plans and number on the waiting list.

5.39 The standard contracts require the NGO to report on staff related information such as number, staff/client ratios, and training. In 9 of the 16 NGO files we examined, there was no information provided on the NGO's staff. In 12 of the 16 NGO files we examined, there was no information on the NGO's Board of Directors.

5.40 There were 9 contracts where reporting on management processes addressing quality of service in the areas of personnel policies, safety policies, quality improvement plan and case plan reviews, was required as part of the signed agreement. We found this information was not provided in any of the 9 instances.

5.41 Annual reporting requirements are an important part of the agreement with the NGO. The information allows for a comparison of performance achieved in relation to the original performance expectations covered by the agreement. The analysis of this information is important in assessing whether value for money has been achieved.

Recommendation

5.42 The Department should ensure that information is received from each NGO on a timely basis as required in the funding agreement. This information should be used by the Department to assess the services provided by the NGO in relation to the original performance expectations covered in the funding agreement.

Departmental Reporting

5.43 Given the significance of the grants provided to NGOs by the Department, we expected the Annual Report of the Department of Social Services and Seniors to the Legislative Assembly would include information on the nature and amount of funding to NGOs.

5.44 We reviewed the 2006-07 departmental annual report for information on grants to NGOs and found there was minimal information reported. There are three Divisions in the Department that provide grants to NGOs. The Social Programs Division was the only division in the Department that provided any reporting on grants to NGOs and it only reported the number of NGOs that received funding through that Division.

Recommendation

5.45 The Department should include additional information on grants to NGOs in its Annual Report to the Legislative Assembly.

MANAGEMENT RESPONSE

5.46 Our report was discussed with the Department of Social Services and Seniors and a written response will be provided.

6. GOVERNMENT'S INVOLVEMENT WITH NATURAL ORGANIC FOOD GROUP PEI INC.

INTRODUCTION

6.1 Executive Council issued an Order in Council on December 12, 2007 requesting the Auditor General to carry out a special investigation into the financial relationship and transactions between the Province, Natural Organic Food Group PEI Inc. and the related company, Natural Organic Food Group Inc. (Quebec). Under section 14(d) of the Audit Act, the Auditor General shall undertake special assignments or investigations at the request of the Lieutenant Governor in Council.

6.2 Executive Council also directed the PEI Lending Agency to appoint a receiver and to prepare for the possible winding down of the hog plant over a three-month period. On January 11, 2008 the PEI Lending Agency demanded payment of the loan outstanding from NOFG PEI Inc., which at that time amounted to $2,091,000. A claim was filed with the court and the PEI Lending Agency requested the court to appoint a receiver. On January 21, 2008 the court appointed a receiver and manager of the property, assets and undertaking of Natural Organic Food Group PEI Inc.

6.3 Natural Organic Food Group PEI Inc. (NOFG PEI) is a private company and therefore, not directly subject to audit by the Auditor General. However, the PEI Lending Agency did provide working capital loans during the peri of operation of the company and the Department of Agriculture provided grants of approximately $2 million. In addition, Island Investment Development Inc. administers the Provincial Nominee Program, an immigration investment program under which funds were accessed.

6.4 We did not conduct a financial audit on the books and records of NOFG PEI. We did, however, examine financial records related to terms and conditions attached to financial assistance provided by government.

6.5 Throughout our review we received cooperation from senior management of the PEI Lending Agency, the Department of

Agriculture and PEI Business Development Inc. We would also like to acknowledge the assistance and cooperation of the Receiver.

OVERALL COMMENTS

6.6 The PEI hog plant has closed and the building and equipment have been sold. The total loss to government as a result of its involvement with NOFG PEI amounted to approximately $4 million. In this report we present findings and recommendations related to government's management of this file during the period of operation by NOFG PEI. Our review disclosed a number of issues both during the acquisition process and the period in which NOFG PEI operated the plant.

6.7 The funding sources and financing requirements identified in the original business plan for NOFG PEI were significantly changed as a result of negotiations that led to the final Purchase and Sale Agreement.

6.8 The need for significant capital upgrades to the plant in order to meet plant inspection regulations and to improve the efficiency in the kill line was considered critical to the success of the operation but the requirement for capital financing was waived. The final Purchase and Sale Agreement also resulted in increased working capital requirements, including an increase in the price of hogs. A plan was not put in place at that time to address the impact of these changes. This issue, combined with a history of losses at the plant, and a business plan that called for increased marketing expenditures and a transition period to achieve higher margin products contributed to ongoing working capital shortages at the plant.

6.9 During the period of plant operations, Government provided approximately $5 million in financing for the plant. Immigrant investor funds provided an additional contribution of $364,000.

6.10 There was a lack of coordination by government in providing assistance and monitoring the progress of this project. The PEI Lending Agency provided some financing to the project but the Department of Agriculture was the lead on the file even though

assisting and monitoring of a manufacturing and processing operation was not considered within its mandate.

6.11 Monitoring of the project was further impacted by the fact that accounting records were not maintained on an ongoing basis and reliable financial reports were not produced. The state of the accounting records also prevented us from reporting with audit level assurance on the nature and amount of financial transactions between NOFG PEI and various related parties. This information is directly connected to one of the covenants in the working capital loan and also has a bearing on the collection of amounts due from related parties on receivership.

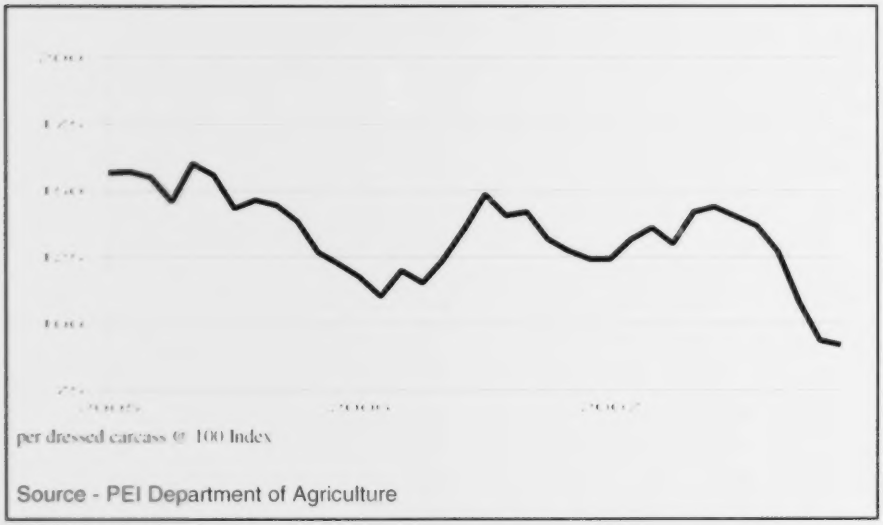
BACKGROUND

6.12 The Prince Edward Island hog industry consists of approximately 130 family-owned farms. The total hog inventory in January 2007 was estimated at 123,500 for PEI. This represented 38 percent of the total Maritime inventory of 322,000 hogs. These figures place PEI with the highest hog inventory in the Maritimes with New Brunswick holding 33 percent and Nova Scotia 29 percent. To put these figures in perspective for the country, the Maritimes held 2.16 percent of the total Canadian inventory of hogs with PEI representing 0.83 percent of the Canadian total. Hog receipts in Prince Edward Island were $27,538,000, $23,630,000 and $20,860,000 respectively for the years 2005 to 2007 which represent 7.5 percent, 6.3 percent, and 5.7 percent of the total agriculture cash receipts for the Province. Hog receipts decreased from 2005 to 2007 by over $6.6 million or 24 percent.

6.13 The market price for hogs is established based on the interrelationship of many factors in a volatile market. Hogs in this region are priced using a formula established on the Chicago Mercantile Exchange (CME) which is based in US dollars. The rise in the Canadian dollar has affected the net price per hog received by the farmer. During the period of operation of the Charlottetown plant by NOFG PEI, some of the lowest market prices for hogs in recent years were experienced. **Exhibit 6.1** illustrates the monthly price paid to PEI producers based on the constructed CME price converted to

Canadian weights and currency. When NOFG PEI was established the hog producers were being paid CME minus $2. Over the period of operation by NOFG PEI, the prices paid to hog producers were increased to the adjusted CME pursuant to the Purchase and Sale Agreement.

EXHIBIT 6.1
PEI BASE HOG PRICES
BEFORE ADJUSTMENTS
PRICE PER CKG



Source - PEI Department of Agriculture

6.14 The Charlottetown hog plant was one of three federally inspected plants in the Maritimes. The other two plants are located in Nova Scotia. According to a consultant's report commissioned by the Department of Agriculture, all three plants were operating well below capacity during 2007: NOFG PEI was estimated to have been working at between 60-86 percent of their 5,000 head per week capacity during 2007. One Nova Scotia plant with a capacity of 6,500 operated at 33-46 percent, and the other Nova Scotia plant with a capacity of 400 head per week operated at 38-75 percent capacity.

6.15 The Charlottetown plant had a single shift capacity of 5,000 hogs per week and at the time of its sale to NOFG approximately 4,000 hogs were being slaughtered per week. These carcasses were broken down into mainly primal cuts for further processing. The plant also produced a fresh sausage line with several varieties. Although

the plant had not been processing beef since 2003, it had the capacity for approximately 200 beef carcasses per week as well. The Charlottetown processing plant was over 20 years old and at the time of its sale was in need of considerable equipment upgrading to improve product quality and consistency.

OBJECTIVES AND SCOPE

6.16 In accordance with Section 14(d) of the Audit Act we conducted a review of the financial support provided by government to NOFG PEI. Our objective was to assess the management processes in place over the provision of assistance, the monitoring of the terms and conditions of the assistance, and the action taken to realize on the security.

6.17 In order to obtain an understanding of the industry and the environment in which the plant was operating we reviewed various industry studies, obtained industry statistics, and interviewed personnel from the Department of Agriculture, PEI Lending Agency, PEI Business Development Inc., representatives of the Producer Association, the Canadian Food Inspection Agency, as well as several shareholders, and various senior management. We reviewed documentation supporting the initial purchase of the plant, as well as each type of financial assistance provided by the Province. We reviewed consultants' studies provided to government. In addition, we reviewed the Receiver's reports and estimated the loss to government as a result of the project.

6.18 There was no financial statement audit carried out in the period during which NOFG PEI was operational and we did not complete a financial statement audit on NOFG PEI. However, we did review documents on file at the plant primarily related to cash and bank records as well as intercompany transactions.

6.19 Our examination was performed in accordance with the assurance standards encompassing value for money as established by the Canadian Institute of Chartered Accountants and accordingly included such tests and other procedures as we considered necessary in the circumstances.

DETAILED AUDIT OBSERVATIONS

Purchase of the Plant

6.20 On April 28, 2006 the former owner sold its 51 percent equity interest in the Garden Province Meats Plant (GPM) for $1 to the other shareholders in the plant representing hog producers and beef producers. After this transfer of shares the hog producers association owned 80 percent and the beef producers association owned 20 percent of the shares of the plant. At that time these shareholders, along with the provincial government, had determined that it was in their collective best interest to have the GPM plant continue to process hogs as the hog production sector was integral to the continued success of PEI's agricultural economy.

6.21 The Hog Commodity Marketing Board established a Transition Team to seek expressions of interest to manage and/or invest in the GPM plant. The team consisted of two deputy ministers and a financial consultant.

6.22 A Request for Expressions of Interest (REI) was issued and widely distributed. The objective of the REI was to enter into a contract with an entity to carry out the day to day operations of the plant. In addition to achieving a contract with an organization willing to operate the facility, the Transition Team indicated they would also be interested in identifying an organization which would be interested in making an equity investment in the plant.

6.23 Four submissions were received and reviewed. The Transition Team then recommended moving to a formal Request for Proposals (RFP) with two of the proponents invited to submit proposals. Only one of the two selected actually submitted a proposal. The recommendation of the Transition Team was to pursue this proposal and to follow a process of due diligence and negotiation. The Hog Commodity Marking Board established a Negotiating Committee, including members of the hog producers association with the assistance of the financial consultant involved in the Transition Team.

The Successful Proposal

6.24 The successful proposal was received from a company based in Quebec in partnership with a company directed by four Island hog producers. The direction of the original business plan was to develop differentiated pork products, including omega, natural and organic and develop the markets for these products. The plan was predicated on the projected growth in the market for differentiated food products. At that time the Quebec group had experience and knowledge in brand development and had labels and registered brands that could be used for PEI pork. A key element of the business plan was that the Quebec shareholders would provide the marketing program to place this pork into the optimal retail venues.

6.25 A positive aspect of the PEI Industry was that the quality of the breeding stock was high. The environment was relatively closed and with foresight the industry had controlled imports of breeding stock and semen. A minimal disease program was established several decades ago which consisted of a nucleus purebred breeding herd and a number of multiplier breeders who generated the high health pigs that improved the industry's rate of performance and substantially reduced the use of medications. This made PEI a good fit to move toward a differentiated product.

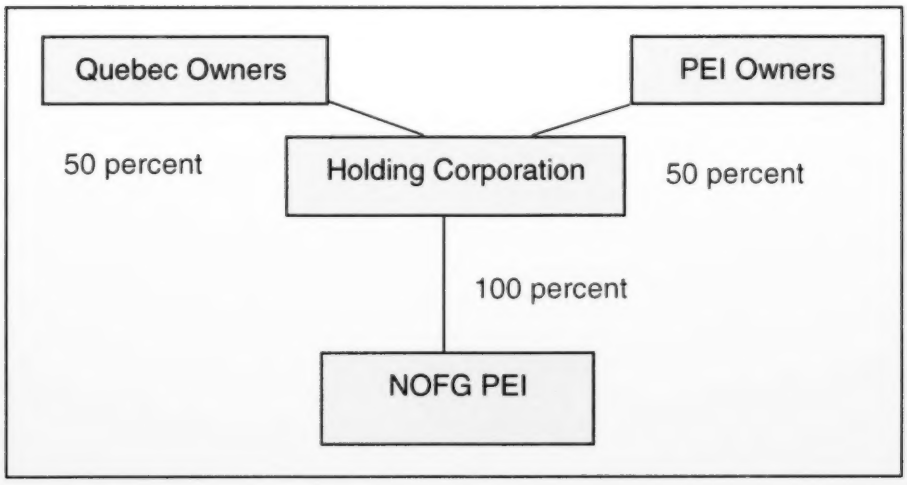
6.26 The PEI group had farm level knowledge and the producer network to motivate PEI and other Maritime farmers to produce differentiated pork. The key to a differentiated model is the traceability of the product line and on-farm adherence to specified production protocols. With experience through their involvement in specified pathogen free breeding stock, it was felt they could extend this to producers of differentiated pork.

6.27 The RFP information document included a section which identified plant upgrades that were critical to the viability of the plant. Some were related to quality improvements that were necessary to increase the availability of quality product for higher margin markets. The second were upgrades required to maintain licenses under the Canada Food Inspection Agency and the United States Department of Agriculture. The business plan proposed included taking an

ownership position in the plant and carrying out the capital improvements to achieve the upgrades indicated in the RFP.

6.28 The ownership structure for the project was established by the PEI group and the Quebec group forming a holding company in which they were equal partners, each owning one share. The holding company purchased the shares of Garden Province Meats Inc. from the previous shareholders. The corporation that was Garden Province Meats then obtained a change of name to NOFG PEI. **Exhibit 6.2** illustrates the ownership structure of NOFG PEI.

EXHIBIT 6.2
OWNERSHIP STRUCTURE - NOFG PEI



Due Diligence

6.29 Although the sale of the plant was carried out between the companies owned by producer organizations and the interested purchaser was a private corporation, government was intricately involved. Government had outstanding loans to producers which at that time were in excess of $7 million. The consensus was that the future viability of the hog industry in PEI was reliant on the continued operation of the hog plant. In addition, it was understood that the proponents for the purchase of the plant would be seeking financial support from government.

6.30 We expected the due diligence carried out on the request for assistance to include, among other things, a consideration of the following factors: an evaluation of the business plan, a review of the management ability of the proponents, an assessment of the risks and any mitigating factors, a financial assessment of the company and proponents, and an evaluation of available security.

6.31 We found that government, through the Transition Team and the subsequent involvement of the PEI Lending Agency addressed many of the issues required in a project evaluation. The education and experience of management were considered. The proposed marketing plans and strategies were examined and marketing staff at PEI Business Development Inc. were requested to provide assurance the marketing approach was reasonable. Credit checks were carried out on the proponents, and security for requested working capital assistance was evaluated.

6.32 The business plan provided was based on the creation of a niche market for omega, natural and organic pork. The business plan indicated that there was a potentially large market for these products which could attract higher returns in the marketplace than commodity products. The Prince Edward Island plant was having difficulty competing with large plants supplying the commodity market. The development of these products was viewed by many in the industry as the only viable option for a small processing plant.

6.33 Producers accepted this model and in general agreed to begin to take steps which would result in changes to on-farm protocols to allow hogs produced on PEI to achieve the status of omega, natural and organic. This change in production requirements would take a period of time with omega being the shortest at six weeks to organic production of hogs which could take up to 3-5 years. The business model put forward was a three-pronged approach including:

- extensive work with hog producers to develop protocols, encourage and support the conversion of on-farm practices, and achieve production of increasing numbers of omega, natural and organic hogs;

- extensive work in market development and brand identification to develop markets for PEI omega, natural and organic pork products as well as continued work in value added product development for this differentiated pork; and
- plant and production upgrades to increase efficiency and convert to increased omega, natural and organic production.

6.34 The long-term goal of the business plan was to eventually construct a value added processing facility which would further process this differentiated pork into omega, natural and organic consumer products.

6.35 The GPM plant had been operating for 20 years and had experienced losses. The plant itself was 20 years old and at the time of the RFP, there were outstanding compliance issues with the Canadian Food Inspection Agency (CFIA) and the US Department of Agriculture (USDA) regulations which would require substantial capital investment to address. This, in addition to capital improvements needed to increase operational efficiency, was estimated to require $2.8 million in capital upgrades.

6.36 The business plan anticipated the capital requirements to be met through a $1 million forgivable loan provided by government with a $1.1 million term loan from Farm Credit Corporation and an equity investment of $700,000 from the proponents. These sources of capital financing did not materialize.

6.37 Similarly the business plan called for an increase in marketing costs to the extent of $2 million per year to develop brand identification and market opportunities for the differentiated products. These would be largely funded through incentive grants to be provided through provincial or federal programs. These additional operating incentives were not received.

6.38 **Exhibit 6.3** illustrates the planned sources and uses of funds for capital and operating improvements in the business plan.

EXHIBIT 6.3
SOURCES AND USES OF FUNDS
NEW INITIATIVES IN THE BUSINESS PLAN
(Millions)

Use of Funds-Capital		**Source of Funds - Capital**	
Equipment and plant renovations	$2.8	Equity Investment	.7
		FCC Loan	1.1
		PEI Forgivable Loan	1.0
			$2.8
Use of Funds-Operations		**Source of Funds-Operations**	
Market Development	$2.0	Innovative and development tax credit or similar provincial or federal program	$1.7

6.39 We found that as negotiations on the agreement of purchase and sale were carried out, key aspects of the financial requirements of the project changed from what was included in the original business plan provided in response to the Request for Proposals. These critical changes in the anticipated sources and uses of funds were not given adequate attention prior to approval of the project.

6.40 There was an extensive negotiation process and a Purchase and Sale Agreement was settled on September 27, 2006 with an amendment on October 2, 2006. The final Purchase and Sale Agreement was significantly different from the business plan submitted and is illustrated in **Exhibit 6.4**.

EXHIBIT 6.4
COMPARISON OF THE BUSINESS PLAN AND THE TERMS OF NEGOTIATED PURCHASE

Business Plan		Purchase and Sale Agreement	
Capital		Capital	
• Capital Improvements Required	$2.8 million	• Requirement for Capital Financing Waived	
Effect on Working Capital		Effect on Working Capital	
• Share price	$1	• Share price - cash	$200,000
		Return on equity $1.53 x 200,000 estimated hog throughput (year 1 of 3 year commitment)	$306,000
• Hog Price: Maintain hog price at previous operators price CME less $2	$0	• Hog Price: Stepped increase to CME x 200,000 estimated throughput (year 1)	$267,000
• Maintain producer payments at one week after delivery	$0	• Producer payments same week as delivery (one time)	$650,000

6.41 As can be seen from the Exhibit, the Purchase and Sale Agreement that was negotiated reflected a significant change in capital funding and working capital requirements. There was no plan put in place to address the impact of these changes.

Capital Financing

6.42 An initial risk facing the project related to lack of financing in place at the outset. The need for capital upgrades was noted in the RFP. The proponents indicated the need for $2.8 million to complete the capital upgrades. When the capital was not in place at the time of completion of the agreement of purchase and sale, Government

waived this as a requirement on the assurances that the proponents would continue to seek external financing.

6.43 At that time the Department of Agriculture indicated that it was essential the capital financing be acquired and without the investment in the short or medium term the plant would not be successful. They also noted that the capital financing was not likely to be available until the plant operations could be turned around. It was likely the Province would be approached to provide the required financing in six to eight months and personal guarantees of the proponents were taken in anticipation of the requirement to provide future financing.

6.44 Although the PEI Lending Agency Board approved the full capital financial plan on September 22, 2006 and the Department of Agriculture indicated that the financing would probably be required from government sources, the capital financing was not put in place. The requirement for the proponents to have capital financing in place prior to the close was waived by Executive Council on assurances that the proponents would seek external financing. The effect was that the company was under capitalized. They could not achieve the working capital projected because of poor quality cuts. They could not achieve the operational efficiency because of needed capital upgrades. In addition, there were outstanding compliance issues with CFIA and USDA. This impacted their ability to raise external financing for the expansion to value added processing.

Operational Financing

6.45 The Purchase and Sale Agreement provided for the purchase of shares of the plant in exchange for $200,000 in cash, $100,000 of which was provided to beef producers for the shares held by their association. In exchange for an exclusive three-year supply agreement the purchasers agreed to pay to producers a premium for hogs delivered to the plant. This premium was based on $1.1 million less an adjusted modified net zero calculation as of September 29, 2006. The modified net zero calculation was provided by an arms length third party. This net equity would be paid back to producers on a per hog basis at 40 percent in the first year, 30 percent in the second year and 30 percent in the third year. This premium per hog

amounted to $1.53 per hog during the time of the operations of NOFG PEI.

6.46 In addition to this premium, the hog producers required and obtained a change in the pricing strategy. Under the previous ownership the plant paid a price per hog which was the constructed Chicago Mercantile Exchange (CME) rate less $2 per hundred kilograms. The supply agreement was negotiated as follows: for the first three months the price would remain the same, during the fourth and fifth months it would be adjusted to CME less $1, thereafter it would be CME. In addition, the agreement provided for the hog producers to be paid weekly for hog deliveries in the current week rather than on the week following deliveries.

6.47 The purchase of shares, return of net equity to producers, and the price adjustment resulted in additional working capital requirements of the plant of approximately $770,000 in the first year. Estimates prepared for the Department of Agriculture indicated that the adjustment to the timing of the hog payments resulted in a one time drain on working capital of $600,000-$700,000. These additional working capital needs along with the increased projected expenditures in marketing of $2 million per year meant an increase in working capital requirements of approximately $3.4 million. The project did not receive the working capital as required which meant it was operationally underfunded.

6.48 Given the risk of NOFG's inability to obtain financing and the acknowledged probability that government would be again approached by the company for capital assistance, government should have monitored the progress of the corporation in seeking external financing. In addition, given these known significant estimated increased operational requirements, government, as part of the due diligence should have worked with the corporation to determine how it would meet its operational financing needs up to the point where increased margins from the differentiated products were expected to be realized.

Recommendation

6.49 When government enters into a development project it should ensure that a financial plan is in place to address the financing requirements and sources of funding. Financing risks identified should be monitored.

Government Financial Support

6.50 NOFG PEI took ownership of the plant in October 2006. Over the 15 months during which NOFG PEI operated the plant, government provided financial assistance through several sources as illustrated in **Exhibit 6.5**.

EXHIBIT 6.5
GOVERNMENT ASSISTANCE TO NOFG PEI INC.
OCTOBER 2006 TO JANUARY 2008
($000)

PEI Lending Agency	**Actual**	**Approved**
Working Capital Line of Credit	$1,475	$1,500
Extension #1	350	350
Extension #2	250	250
	$2,075	$2,100
Department of Agriculture		
Working Capital Grants	$1,775	$1,800
Equipment Grants	172	198
Honoring of Guarantee to Producers		
• initial 2 week guarantee payout	729	1,000
• additional weeks pay out	197	-
	$2,873	$2,998
Total	**$4,948**	**$5,098**

Note: Does not include amounts flowed through to producers under the Swine Quality Improvement Program.

PEI Lending Agency - Working Capital $1.5 Million

6.51 On September 21, 2006 a conditional letter of offer was issued to Garden Province Meats (which later became NOFG PEI). The offer included a revolving line of credit of $1.5 million and a guarantee to producers that the Province would provide payment to a maximum of two weeks regular shipments in the event of default by GPM. There were numerous conditions attached to the financing offer:

- the execution of a purchase and sale agreement;
- the provision of a supply agreement by the Hog Marketing Board;
- confirmation of $500,000 cash injection by proponents;
- confirmation of $2.8 million in capital financing;
- security for the line of credit to be a first charge on accounts receivable and inventory and a second charge on plant assets;
- PEI to have the right of first refusal on the value added processing capacity being considered; and
- while the line of credit and bond were outstanding a number of requirements would be in place to limit the action the company could take without the written approval of the PEI Lending Agency.

6.52 The final letter of offer was signed on October 5, 2006 with an amendment on October 10, 2006, and some conditions were altered from the September 21, 2006 conditional offer. Executive Council waived the condition for capital financing to be in place. The PEI Lending Agency was directed to provide a working capital loan of $1.5 million and a guarantee of payment of two weeks shipments to producers up to $1 million.

Department of Agriculture Grant - $398,000

6.53 On May 4, 2007 a request for assistance was received from NOFG PEI by the Department of Agriculture. The plant was due to be audited for compliance with the United States Department of Agriculture regulations which were required in order to maintain its export license. The company needed to demonstrate a commitment to remediate deficiencies noted in the previous USDA/CFIA audit. The company had tried to obtain the required capital financing but was unsuccessful. A memorandum of understanding (MOU) was issued

by the PEI Department of Agriculture for $99,000 related to implementation of Biosecurity measures with terms and conditions set out. The USDA/CFIA audit was conducted on May 24, 2007 and resulted in a Notice to Delist the Facility and revoke the Export license.

6.54 In June 2007 the $1.5 million line of credit provided by PEI Lending was fully drawn down and the plant was in need of additional working capital. A commitment to provide working capital financing had been received from a financial institution if the Province would provide the capital financing. In response to a recommendation from the Department of Agriculture, Executive Council approved $200,000 in working capital to enable the plant to continue operating pending further consideration by the new government. On this same date, a further MOU for additional funding to address the USDA/CFIA audit requirements was signed in the amount of $99,000.

6.55 The two MOUs totaling $198,000 were for the same list of required equipment and upgrades in order to maintain the USDA/CFIA certification. These agreements were divided in two and each approved by the Deputy Minister of Agriculture. The Treasury Board Policy on Delegation of Signing Authority requires Treasury Board approval for contracts exceeding $100,000.

6.56 An accounting firm was engaged in June 2007 to carry out a review and make recommendations on the one month and six month cashflow requirements of the facility, the cash required to implement the planned operational and capital improvements required to remediate the deficiencies identified in the USDA/CFIA audit, and to analyze the disposition of the funds advanced by shareholders and the PEI Lending Agency.

6.57 Under the terms of the MOUs, $50,000 was advanced on signing the first MOU and invoices were to be obtained before additional funding was provided. We found there was approximately $80,000 worth of payments made which did not have the support of an invoice. These payments were made based on quotes and estimates. This represents approximately 50 percent of the total paid under both MOUs.

Department of Agriculture Grant - $1.6 Million

6.58 On July 4, 2007 the Department of Agriculture provided information to Executive Council regarding the financial condition of the plant and the need for additional working capital. The company was requesting working capital to continue to operate and to increase throughput to achieve greater efficiency at the plant. Executive Council approval was obtained for the Department of Agriculture to provide working capital grants to a total of $1.6 million which was designed to allow the plant to continue to operate at current levels. It was anticipated that this infusion of working capital would cover the plant for three months.

6.59 The Department continued to engage an accounting firm to review the cash flow requirements and provide approval on the weekly request for working capital advances.

6.60 We noted that the Executive Council approval stated that the PEI Lending Agency and the Deputy Minister's Working Group on the Beef Plant would be responsible for setting conditions on the disbursement of the funds and approve and track the payments. When we followed up with the PEI Lending Agency we were advised they were not aware of their intended role in this scenario. Although the Department of Agriculture implemented a process whereby an external accounting firm provided oversight for the advance of working capital under the $1.6 million grant, the working group did not establish documented conditions for the disbursement of funds.

PEI Lending Agency - $350,000

6.61 In October 2007 the working capital loan of $1.5 million from PEI Lending Agency was due for renewal. The financial condition of the plant had not improved and the efforts to raise external investment capital in order to address the critical plant upgrades were ongoing. Because of the condition of the plant and the working capital shortage, it was difficult to interest external financiers until the owners could prove the business model would work. The PEI Lending Agency renewed the working capital loan for an additional year and provided an increase to the working capital loan of $350,000 on the approval

of the Board of Directors. This additional funding was provided with a guarantee by the Department of Agriculture that if NOFG PEI could not repay the loan, the Department would cover the loss to the PEI Lending Agency.

6.62 PEI Lending Agency Act Regulations Section 2(1) states that *The Agency may, with the approval of the Board, advance any loan to any person where the total indebtedness of the person, including guarantees provided on behalf of that person or affiliate does not exceed $2,500,000 in the aggregate. Section 2(2) requires Executive Council approval for loans in excess of $2,500,000 in aggregate.*

6.63 The original letter of offer to NOFG PEI by PEI Lending Agency provided for a $1.5 million working capital loan and a guarantee of up to $1 million. These total $2.5 million in exposure to this client. Therefore, the additional working capital of $350,000 should have been approved by Executive Council.

PEI Lending Agency - $250,000

6.64 In December 2007 the plant was struggling to meet producer payments and a further increase to the working capital loan was approved for $250,000. This again was provided by the PEI Lending Agency with a letter of guarantee from the Department of Agriculture. In this case the additional financing was approved by the CEO of the Lending Agency with the intention of receiving ratification by the Board of Directors at the next Board meeting. Before the next PEI Lending Agency Board meeting was held, the government announced they were no longer supporting the plant. This additional working capital was never ratified by the Board of PEI Lending Agency and was not approved by Executive Council.

6.65 Although the Department of Agriculture provided a letter of guarantee to PEI Lending Agency, the total exposure exceeded the $2.5 million approved in the original letter of offer. These two additional loans amounted to $600,000 bringing the exposure through loans and guarantees to $3.1 million.

Recommendations

6.66 Financial assistance provided by the PEI Lending Agency should be approved in accordance with the Lending Agency Act Regulations.

6.67 Invoices should be obtained prior to advancing funds for equipment acquisition.

6.68 Responsibilities outlined by Executive Council regarding the disbursement of financial assistance should be followed.

Compliance With Terms and Conditions of Financial Support

6.69 Financial assistance provided by government normally includes terms and conditions to ensure the recipient uses the assistance for the purposes intended and to reduce the risk to public funds. We expected the PEI Lending Agency and the Department of Agriculture to impose terms and conditions on the financial assistance they provided and to monitor compliance with those conditions. Our audit procedures included an assessment of compliance with the terms and conditions agreed to by NOFG PEI and government.

PEI Lending Agency

6.70 The loan agreement included security and other conditions which had to be met prior to the closing of the transaction, specific negative covenants which were to be complied with during the time the loan was outstanding, as well as specific reporting requirements during the period of the loan agreement.

Security Requirements

6.71 The security required in the letter of offer included:

- a promissory note for $1.5 million;
- a general security agreement of $2.5 million;

- a first security interest over all inventory and accounts receivable and a second security interest over personal and real property of the borrower including land, buildings and equipment which on or before December 31, 2006 shall become a first security interest;
- a $2.5 million corporate guarantee from each of the Quebec company, the PEI company and the holding company;
- personal guarantees of five proponents in the amount of $50,000 each; and
- fire insurance coverage.

All of these security requirements were in place prior to release of the working capital loan.

Negative Covenants

6.72 The loan agreement included specific negative covenants to limit the action the borrower could take without the written consent of the Agency. One of these covenants stated that the borrower would not permit outflows of funds to an affiliate or related company, their shareholders or directors. This would include but was not limited to redemption of shares, payment of dividends, extension of loans or similar outflows. The agreement states that consideration for payment of dividends and bonuses would be given by the Lending Agency upon satisfactory review of the financial statements. We carried out various audit procedures to assess compliance with this covenant.

6.73 At the outset of our audit work we noted that the financial records of NOFG PEI included accounts receivable from related companies with general ledger balances as indicated in **Exhibit 6.6**. We attempted to substantiate the balances in these intercompany accounts to determine the amount and nature of any outflows to related parties. Due to the incomplete financial records we cannot provide an audit level of assurance that the account balances are correct. For example, we became aware that NOFG PEI had entered into a contract with the PEI owners whereby an amount would be paid for each omega, natural and organic hog purchased by the plant. In addition, $1 per hog would be paid for specific services provided. We found that due to the financial pressures at NOFG PEI payments to the PEI owners ceased and the remaining amounts payable were not

recorded in the financial records. There was no record of this contract at the plant and we only became aware of it during interviews. There could be other contracts in place that were not reflected in the accounting records.

EXHIBIT 6.6
GENERAL LEDGER BALANCES
INTERCOMPANY LOANS
AS AT JANUARY 2008
(unaudited)

Accounts Receivable by NOFG PEI from:	
Quebec Company - owners	$(306,339)
PEI Company - owners	(16,903)
Holding Company	499,541
Consultant Company owned by a shareholder	336,190
	$ 512,489

6.74 Given the condition of the accounting records, we then began reviewing the bank statements of the Company to gain an understanding of its cash flows. We were particularly focused on those transactions that may violate the covenants in the agreement.

6.75 In our review of cash transactions, we focused on payments to related parties, to Quebec vendors, and to other non-operational vendors. We conducted an extensive review of cash transactions. We reviewed the cheque listings of all bank accounts to identify payments made to selected vendors and examined supporting documentation where available. To ensure our review of payments was complete, we also reviewed all non-cheque withdrawals, such as wire transfers from each bank account. Again, we looked for backup to substantiate those transactions. Finally, we looked for backup supporting the deposits into each of the bank accounts.

6.76 We focused our review on the cash transactions as we had concluded the accounting records of the Company were largely unreliable. The accounting records of the company had never been

audited, the position of controller had been vacant for months, bank reconciliations had not been done for an extended period, and many adjusting entries had no supporting backup available for review. The fact that there were no accounting personnel on site made our review that much more difficult.

6.77 As a result of our work on cash transactions, we found that bonuses were paid in the amount of $10,000 to each of the Vice President of Finance and the President of NOFG PEI without the approval of PEI Lending Agency. This is a specific contravention of the terms of the loan agreement.

6.78 Although we could not substantiate intercompany balances, we noted several instances where transfers were made from NOFG PEI to related companies that require further comment. During the operation of NOFG PEI wire transfers of $240,000 were made directly to the loan account of the Quebec company. These amounts reduced the outstanding payable to the Quebec company. The payable to the Quebec company arose mainly as a result of a branding and marketing agreement which was in the normal course of business.

6.79 There was an amount of $336,000 paid by NOFG PEI to a consulting company owned by the President of NOFG PEI. This amount was set up as an advance to the consulting company that was receivable to NOFG PEI. This loan to a related party does not appear to be in the normal course of business operations and should therefore have been approved in advance by the PEI Lending Agency under the terms of the loan agreement.

6.80 The numbered company acted as a holding company on behalf of the Quebec owners and the PEI owners. There was an amount of $345,000 advanced to the holding company which was used by the holding company to acquire the hog plant including payment for the shares and legal fees. PEI Lending Agency was not specifically requested to approve this advance to a related company. However, it appears that government was aware that the funds would be used in this manner.

6.81 Most of the Senior Management of NOFG PEI were located in Quebec during its period of operation. Although efforts were made to hire a local controller, a suitable candidate was not found. Management personnel were paid a combination of salary, bonuses, and consulting fees in some cases. In addition, management was reimbursed for travel costs. These reimbursements would not include payments made directly by NOFG PEI to travel vendors. As part of our work we examined all payments for travel, salary and consulting fees paid to these personnel. In total these payments were significant. For some travel and consulting fee transactions we could not obtain supporting documentation. **Exhibit 6.7** illustrates the compensation to four senior management personnel broken down by type of payment.

EXHIBIT 6.7
PAYMENTS TO NON-RESIDENT
SENIOR MANAGEMENT OF NOFG PEI
FOR THE 16 MONTHS ENDED JANUARY 30, 2008
($000)

Salary	$ 442
Bonus	20
Consulting Fees	234
Travel Reimbursements	348
Total	**$1,044**

6.82 The operation of a kill and chill facility requires extensive working capital. Large amounts of cash are required to purchase hogs on a weekly basis. To the extent that the cash raised in PEI either through the working capital loan or through normal turnover of accounts receivable was transferred to other affiliated organizations, it was not available for operations. These intercompany transactions affected the cash flows of an already cash strapped company to the point where it increased the requirement for assistance from Government.

Financial Reporting

6.83 The loan agreement with the PEI Lending Agency set out a number of reporting requirements. NOFG PEI was to provide to Lending, within 15 days of the end of each month, the monthly interim financial statements including an income statement, balance sheet, aged listing of payables and receivables, margin calculation and summary of inventory. A copy of the audited financial statements was to be provided 120 days after the fiscal year end.

6.84 The Lending Agency did not receive any interim financial statements during the period when the loan was outstanding. When the former owners of the plant left, the accounting system was dismantled. A contract for a new system had been entered into and was required to be honored by NOFG PEI pursuant to the agreement of purchase and sale. This new system required complete set up and a rebuild of accounts from April 2006 to the date they took possession in October 2006. Just after NOFG PEI took ownership of the plant, the controller resigned. This meant the company was faced with limited financial experience and a new system that needed to be implemented.

6.85 Management of the plant tried to hire a new controller and engaged the assistance of a Human Resource group but was not successful. The company obtained accounting assistance from local firms and worked to set up the financial accounting system. Under these conditions the regular monthly financial statements were not produced until the spring of 2007.

6.86 Audited financial statements were not produced. The year end for the NOFG PEI plant was September 30. The first year end therefore was September 2007 with closing entries prepared in October. By that time the plant was in severe financial difficulty and no audit was carried out.

6.87 The PEI Lending Agency did receive a margin statement each month signed by the Company President and the Vice President of Finance. The margin statement included a statement of the accounts receivable balance and the inventory balance as well as a calculation

of the loan based on the percentage of outstanding accounts receivable and inventory. These statements were late seven out of twelve months. Due to problems with the accounting system, we could not trace the accounts receivable and inventory balances which were reported to the Lending Agency to the financial accounting records at NOFG PEI.

6.88 The letter of offer states that the working capital loan shall not exceed 75 percent of the accounts receivable balance and 50 percent of the inventory balance. We noted that the working capital loan was out of margin for three months, June, July and August of 2007. Lending Agency staff followed up as required.

6.89 Given the fact that NOFG PEI did not provide monthly financial statements during the period of operations, we considered what additional action PEI Lending Agency could have taken to monitor the loan. We noted that a contingent condition of the loan was the right for the Province to appoint a voting member to the Board of Directors of the company. This condition was not exercised.

Department of Agriculture

6.90 Similar to the loan agreement, the agreements in place over the financial assistance provided by the Department of Agriculture also included reporting requirements. The two MOUs for Biosecurity and USDA/CFIA certification required a final report and reconciliation to be provided by NOFG PEI to the Department of Agriculture. This report was not provided and there is no indication that the Department followed up with the company to obtain it.

6.91 The $200,000 grant, that was provided to the company in June 2007 to allow the plant to continue to operate until the new government had an opportunity to consider the situation at the plant, had a condition attached to the funding that all functions related to NOFG PEI currently based out of Montreal would be reassigned to Charlottetown. This condition was not followed up by the Department.

6.92 In addition to these grants, the Department of Agriculture had a Swine Quality Improvement program (SQIP) which had existed under the plant when it was operated by the former owners. This program provided a premium to hog producers if their hogs met certain quality requirements. The program was administered through the plant. Although this program acted as a flow through from the Department to producers, the total amount allowed each year was provided by the Department in advance to NOFG PEI. Two lump sum payments totalling $400,000 were made for 2007-08. If the grant exceeded the amount required to be paid out to qualified producers, then any excess was to be paid back to the Department. Although this is a flow through grant to producers, it affected the working capital available to the plant for operations. The Memorandum of Understanding for the SQIP required monthly reports on the number of qualifying hogs and the amount paid out. We found the Department was not receiving these monthly reports from NOFG PEI and did not follow up. Therefore it is not clear if all the SQIP funds received by NOFG PEI were fully disbursed to producers.

Recommendations

6.93 If required financial statements of a client company are not available, compensating controls should be implemented such as reviewing other types of reports and/or exercising a right to appoint a representative to the Board of Directors.

6.94 The Department of Agriculture should ensure that terms and conditions attached to financial assistance are complied with.

Coordination of Government Involvement

6.95 Given the impact of this project on the hog industry in PEI and the involvement of various government agencies including the Department of Agriculture, the PEI Lending Agency, and the PEI Business Development Inc., we expected the business relationship between NOFG PEI and the Government to be coordinated with clear lines of authority.

6.96 In the early stages of the development, the Transition Team was established consisting of the Deputy Minister of Agriculture, the Deputy Minister of Development and a financial consultant. Early on, the Deputy Minister of Agriculture became the lead on the file. When negotiations were well under way, the PEI Lending Agency was approached in August 2006 to act as the vehicle for the government financing that would be provided. We were advised that the PEI Lending Agency did not carry out the normal project evaluation on this file because many of the aspects had already been negotiated. Although the Lending Agency had input into the letter of offer, and the offer was approved by the Lending Agency Board of Directors, from Lending Agency's perspective they had been directed to provide the financing and had not been provided access to all aspects of the original business plan.

6.97 In October 2006 when the plant changed hands, government waived the condition for the proponents to have financing in place for the capital upgrades required at the plant. The submission to Executive Council indicated it would be unlikely the proponents would be able to raise external financing and government would be required to provide the financing within six months. The PEI Lending Agency advised they were not party to this submission although they were advised the requirement was waived. When NOFG PEI approached the Department of Agriculture in May 2007 for assistance to retain the USDA/CFIA certification, the Department was concerned that financing had not been obtained and upgrades had not been made. We were advised that the Department of Agriculture did not see their role as one of monitoring the progress of this project.

6.98 In July 2007 when the $1.6 million working capital grant from the Department of Agriculture was approved, the PEI Lending Agency had a working capital loan of $1.5 million outstanding. The Lending Agency was not party to the request for additional operating assistance for the plant put forward by the Department of Agriculture. The information provided to obtain the financing indicates NOFG PEI had obtained an offer to finance the working capital requirements of the company by an external financial institution if government would finance the capital upgrades to the plant. It does not appear that this financing offer was thoroughly assessed by government.

6.99 In June, July and August of 2007, external accounting staff were engaged by the Department of Agriculture to monitor and oversee the advancing of working capital under the $1.6 million grant approved by Executive Council. We were advised these services were purchased because it was not in the normal course of business for the Department of Agriculture to monitor the disbursement of working capital grants to private companies. However, government has expertise and experience in this area through both PEI Lending Agency and PEI Business Development Inc.

6.100 This project was an economic development project. The plant itself had existed for 20 years and in that respect it was not new, however, the business plan to develop differentiated products and value added processing of pork was new. The proponents were trying to develop new products and new markets related to the pork industry. The adaptation of the plant to new processes and the upgrades for the kill line to improve product quality were necessary for the continued operation of the plant. Government has an economic development section with expertise and experience in economic development initiatives.

Recommendation

6.101 To ensure economic development initiatives are thoroughly assessed and monitored there should be coordination among departments and agencies keeping in mind their respective mandates and areas of expertise.

Guarantee to Producers

6.102 The financial assistance provided by government included a surety bond of up to $1 million. The surety bond was to provide comfort to hog producers and it would guarantee to producers that sufficient funds would be available to pay for a maximum of two weeks regular shipments in the event of a default by NOFG PEI. If the PEI Lending Agency was required to pay this out, all costs would then become part of the debt owed by NOFG PEI.

6.103 The guarantee by government to producers was a requirement established early in the negotiation process for this project. The Executive Council approval included this guarantee. Although it was agreed to by all parties in the signed letter of offer, we were advised that the bond document was not prepared.

6.104 Even though there was no surety bond document drawn up, the terms and conditions of the guarantee were established in the original letter of offer which was agreed to by all parties. Therefore, the requirement to pay the amount of two weeks regular shipments up to $1 million to producers was binding.

6.105 According to the letter of offer, the Bond was subject to an annual fee of 1 percent which is the normal guarantee fee required by PEI Lending Agency. We found that this administration fee was not collected by PEI Lending Agency.

6.106 When the plant was placed into receivership in January 2008 there were a number of producers that were owed money for hog shipments. The Department of Agriculture obtained a list of outstanding amounts due to hog producers from the Receiver. On January 25, 2008 the Department paid out $729,000 in payments to producers for the two weeks of shipments prior to plant closure. A subsequent payment of $197,000 was made to producers to pay out all outstanding amounts owed to producers by the plant. This subsequent payment was not approved by Treasury Board or Executive Council.

6.107 The first payment to producers to cover the two weeks shipments was agreed to in the initial letter of offer. When the plant ceased operations government was required to honor its commitment. However, the additional $197,000 paid out to producers for additional weeks was not required under the terms of the agreements. For shipments beyond the two weeks covered by the guarantee, producers became unsecured creditors. There are a number of unsecured creditors who have sustained losses as a result of the closure of the plant. Decisions such as this to provide additional support over and above what was agreed to at the time, should only be entered into after consideration of the full context of the impact on

affected parties. The original guarantee was approved at the Executive Council level and therefore, changes to that guarantee should have been made at the same level.

Recommendation

6.108 The Department of Agriculture should ensure changes to terms and conditions attached to financial assistance are authorized at the level of the original approval.

Investments by Proponents

6.109 The initial business plan set out a personal investment by the shareholders of $700,000 in equity. In the final loan agreement provided to the proponents this requirement was revised to a $500,000 cash injection. During negotiations there is evidence that the shareholders indicated they did not have equity to invest in the project.

6.110 In order to satisfy the cash injection requirement, the proponents applied for funding under the Provincial Nominee Program which is administered by Island Investment Development Inc., an agency of government. Under this program there is a time lag between approval of a company and the receipt of funds through investment units. Therefore, NOFG PEI entered into a mortgage as a bridge financing arrangement which was to be repaid as the immigrant investment funding was received.

6.111 The mortgage was secured by a first charge on the plant and equipment of NOFG PEI. Under the terms of the letter of offer, the Lending Agency agreed to take a second position security on the land, building and equipment. On or before December 31, 2006, the first position security held by the third party lender to secure the $500,000 mortgage was to be satisfied or postponed to the interest of the Lending Agency. If NOFG PEI could not retire the debt at December 1, 2006 then the PEI owners, the Quebec owners, and the numbered company were required to retire the debt to allow the Lending Agency to obtain first position.

6.112 There are several issues with this arrangement. The letter of offer required evidence of the shareholders' cash injection of $500,000. This amount was provided pursuant to the $500,000 mortgage but it was secured using the assets of the company being acquired, i.e., NOFG-PEI. The mortgage carried an interest rate of Bank of Canada prime rate plus 4 percent. The interest on the outstanding balance was paid by NOFG PEI with a portion set up as receivable from the Quebec owners and the numbered company. In addition, a fee of $50,000 was taken by the financing company and when the mortgage was not fully paid out by December 31, 2006 an extension fee of $57,500 was paid by NOFG PEI but was again set up as receivable from the Quebec company and the numbered company. **Exhibit 6.8** illustrates that although the loan agreement required a $500,000 cash injection by shareholders the net cash injection to NOFG-PEI was $403,900. In addition, $345,000 was advanced to the holding company to cover the purchase of shares and other costs associated with the purchase of the plant.

EXHIBIT 6.8
CASH INJECTION
REQUIRED BY LOAN AGREEMENT

Mortgage Financing		$500,000
Less: Amounts paid by NOFG PEI		
Interest on Mortgage	$38,600	
Extension Fee	57,500	(96,100)
Net Cash Injection		$403,900

6.113 The Provincial Nominee Program is a Federal/Provincial program designed to expedite immigration for individuals and their families who meet the criteria for the following initiatives:

- increased business and economic development;
- increased supply of skilled workers;
- increased population; and

- achievement of provincial demographic social and cultural objectives.

Under this program eligible immigrants invest in local companies, and in exchange the processing of their visa through Immigration Canada is expedited.

6.114 The PEI owners and NOFG PEI applied for and were approved to receive four investment units each which were applied against the mortgage. We did not audit the Provincial Nominee Program. However, we obtained and reviewed documentation on the net cash received through the program.

6.115 Government approved the use of the Provincial Nominee Program to pay out the bridge financing arranged by the shareholders. The investment units provided to the recipient company were expected to amount to approximately $55,000 each. This multiplied by eight units is $440,000 which indicates a known shortfall of $60,000 in retiring the mortgage. There was no indication of where this money was going to come from. In addition, when the units were acquired there was a commitment fee of $50,000 related to the mortgage as well as additional legal fees and settlement fees extracted from the units up front, so that NOFG PEI received less than $55,000 per unit. The loan agreement required the mortgage to be settled by December 31, 2006 to allow Lending Agency to obtain first position security. When that date arrived, NOFG PEI could not pay the balance due and the PEI Lending Agency did not receive first position security as required.

6.116 Exhibit 6.9 illustrates the net cash received through the Provincial Nominee Program and the shortfall on settlement of the mortgage. PEI Lending Agency was required to pay out $142,000 to satisfy the mortgage. This amount was added to the outstanding debt of NOFG PEI.

EXHIBIT 6.9
NET CASH AVAILABLE
TO SATISFY MORTGAGE

Mortgage Balance		$500,000
Less:		
Provincial Nominee Receipts:		
8 Units x 55,000	$440,000	
Legal Fees	(21,400)	
Settlement Fees	(5,000)	
Commitment Fee-Mortgage	(50,000)	(363,600)
Add:		
Accrued Mortgage Interest to Date of Payment		5,600
Amount paid by PEILA		$142,000

6.117 Personal guarantees were signed by five Directors and pledged as security for the loan agreement with the PEI Lending Agency. These personal guarantees are held by the PEI Lending Agency.

6.118 As part of the required security for the $1.5 million working capital loan and the $1 million guarantee to the hog producers, corporate guarantees of $2.5 million were signed by the holding company, the Quebec company and the PEI company. For the PEI company and the holding company an additional certificate was provided stating that if the company was required to pay out the guarantee it would still have assets sufficient to meet its liabilities.

6.119 We were advised that Lending Agency will consider its action under the guarantees when the total loss to the Agency is finalized and the Receiver's final report is issued.

Recommendation

6.120 PEI Lending Agency should assess the recourse available in exercising the remaining security for the loan.

Branding and Marketing

6.121 It was stated in the original business plan that the Quebec company would be the marketing arm of the organization. Prior to its involvement with the PEI plant, the Quebec company was working on developing and registering a number of omega, natural and organic brands and trademarks.

6.122 On October 20, 2006 NOFG PEI signed a Trademark and Marketing Licensing Agreement with the Quebec company. This contract related to five trademarks that were developed or were under development. The contract allowed NOFG PEI to use these trademarks and related expertise of the Quebec company in exchange for $487,500 up front and a royalty of 0.5 percent of net revenues up to the first $100,000,000. In addition, NOFG PEI agreed to pay all out of pocket costs of the Quebec company. Up to the end of September 2007, there were $160,000 in royalties set up as payable to the Quebec company under this agreement.

6.123 Given that the letter of offer required written approval by the Lending Agency for cash outflows not in the normal course of business, we assessed the Trademark and Marketing Licensing Agreement to determine whether the nature and amount of payments arising from the contract were reasonable and in the ordinary course of business.

6.124 We found there was no supporting documentation to substantiate the valuation of the branding asset at $487,500. We were advised that this amount was arrived at through discussion and negotiations. We subsequently determined that this type of arrangement including a royalty fee is not unusual and the valuation arrived at is not unreasonable.

6.125 Although the branding asset was set up as an asset on the records of NOFG PEI, it would not have a liquidation value for receivership purposes as the Agreement that gave rise to the asset provides an exclusive license for use but not title to the brands developed.

Receivership

6.126 The Quebec group was working with a securities firm to raise private capital for the operation. A letter indicating that work was underway in this regard was sent to the Department of Agriculture. On December 11, 2007 Executive Council met to address a request by NOFG PEI for additional working capital assistance to continue operations until the first tranche of investment capital was anticipated, which was expected to arrive the end of January 2008. The decision was made to decline the request and direct PEI Lending Agency to move to appoint a Receiver.

6.127 On December 13, 2007 the government publicly announced that it was no longer supporting NOFG PEI. The shareholders of NOFG PEI offered the plant to government but it was not accepted. Finally on January 18, 2008 the PEI Lending Agency was notified that the plant could no longer continue to operate. On January 21, 2008 PEI Lending Agency, as the holder of the security, applied to the court to have a Receiver appointed.

6.128 The Receiver was appointed by the court on the recommendation of the PEI Lending Agency. The Receiver took control of the plant and operated as a going concern for a brief period. A request for expressions of interest to acquire the plant was issued by the Receiver and no offers were received. On the Receiver's recommendation the plant ceased operations on March 28, 2008.

6.129 Upon closure of the plant, the Receiver took action to liquidate the land, buildings and equipment to the benefit of the secured creditor, PEI Lending Agency. Once the Receiver was appointed, the relationship between the Receiver and Government was managed through the PEI Lending Agency. As of September 30, 2008, the

Receiver provided three reports based on activities carried out under the receivership. All three reports were filed with the court.

6.130 Exhibit 6.10 illustrates the amounts paid out by government and the recoveries as a result of the receivership.

EXHIBIT 6.10
NOFG-PEI INC.
ESTIMATED LOSS TO GOVERNMENT
($000)

Government Assistance to NOFG-PEI Inc.		
PEI Lending Agency	$2,075	
Department of Agriculture	2,873	
		$4,948
Add Costs/Charges		
Accrued interest	20	
Buy out of 1st position on Mortgage (added to debt)	142	
PEI Lending Agency-Legal	81	
PEI Lending Agency-Receiver	192	
Consultant fees	198	633
		5,581
Less Estimated Recoveries		
Estimated receipts - sale of property, auction and collections	1,279	
Estimated disbursements to complete	(386)	
Cash on Hand	385	(1,278)
Estimated Total Loss to Government		**$4,303**

FINANCIAL STATEMENT AUDITS

7. INTRODUCTION TO FINANCIAL STATEMENT AUDITS

INTRODUCTION

7.1 Section 13 of the Audit Act establishes the Auditor General's mandate to perform financial audits of the Public Accounts, Crown controlled or owned corporations, and the trusts and funds held by any agency of government insofar as they are not subject to financial audit by an external auditor.

7.2 Financial statements are management's responsibility and reflect management's assertions. They provide information that is used to make important economic decisions. It is imperative that the reader has confidence in the quality of that information.

7.3 The auditor is independent of management and can objectively assess the accounting principles used and the estimates and other decisions made by management as reflected in the financial statements. An examination of the entity's accounts is carried out in accordance with generally accepted auditing standards. These standards have been established over time and continue to evolve with the changing economic environment. The result of the examination is the auditor's opinion as issued in the Auditor's Report.

7.4 In addition to issuing an Auditor's Report on the financial statements, the auditor may also identify problems in the financial controls and accounting records. In these cases, findings and recommendations are reported in a management letter addressed to the department or agency.

7.5 For the majority of the financial statement audits we performed, management letters were issued. We brought to management's attention any problems noted during the audits and made recommendations for improvements. These recommendations are at various stages of implementation.

7.6 In the following sections we provide summary information on our audits of the Public Accounts and Appropriations.

8. PUBLIC ACCOUNTS

BACKGROUND

8.1 The Public Accounts include the annual financial statements of government and are the primary source of information on government's stewardship of public funds both to Islanders and to the Legislative Assembly.

8.2 The Public Accounts are prepared by the Comptroller and tabled by the Provincial Treasurer as required by the Financial Administration Act. According to the Act, the Public Accounts must contain the Financial Statements of the Operating Fund and the Consolidated Financial Statements of the Province, along with any other statement required by Act to be presented. The Consolidated Financial Statements provide the most complete information about the operating results and financial position of the Province as they consolidate the accounts of the Operating Fund with those of the Crown corporations and agencies.

8.3 The Public Accounts for the year ended March 31, 2008 consist of two volumes:

- Volume I contains the audited consolidated financial statements.
- Volume II contains the audited financial statements of the Operating Fund, Crown corporations and agencies.

OBJECTIVES AND SCOPE

8.4 In accordance with the Audit Act, we performed an audit of the Public Accounts of the Province for the year ended March 31, 2008. The objective of our audit was to express an opinion on the financial position and operating results of Government. Our audit reports on the Consolidated Financial Statements and the Operating Fund Financial Statements for the year ended March 31, 2008 did not contain any qualifications or reservations.

8.5 Under Section 17 of the Audit Act, the Auditor General is not required to audit or report on the accounts of any agency of

government where another auditor has been designated to audit its accounts. In these instances, the Auditor General relies on the Auditor's Report for each of these entities when performing the audit of the Public Accounts.

8.6 This report contains comments and observations arising from our audit of the Public Accounts for the fiscal year ended March 31, 2008.

FINANCIAL HIGHLIGHTS

8.7 The following schedule provides a summary of the consolidated results for the last three years.

	Year Ended March 31 (Millions)		
		Restated*	
	2008	2007	2006
Provincial Revenue	$ 784.5	$ 757.6	$ 725.5
Federal Revenue	517.9	474.4	444.4
	1,302.4	1,232.0	1,169.9
Expense	1,306.0	1,208.1	1,169.2
Annual Surplus (Deficit)	$ (3.6)	$ 23.9	$ .7

* Restated to record gross revenues and expenses of Harness Racing PEI.

DETAILED AUDIT OBSERVATIONS

Financial Statement Discussion and Analysis

8.8 The Public Accounts is a major accountability report of the Province of Prince Edward Island. Its potential is not being maximized, except for four graph presentations government has not included any financial discussion and analysis. For the jurisdictions we reviewed, each of them had a financial statement discussion and analysis section of considerable size that was issued with the Public Accounts.

8.9 The purpose of the financial statement discussion and analysis is to expand on and explain information contained in the financial statements, making them more useful by extending the understanding of the information they report beyond those who possess technical expertise. The information complements and supplements the government's financial statements, allowing the government to express qualitative information given its detailed knowledge of the transactions, events and conditions underlying the reported financial position and changes in financial position. Some basic information one would expect to find in an financial statement discussion and analysis would be:

- a highlights section;
- an analysis section that identifies and explains significant variances between the current year actual results and the budget as well as significant variances between current year actual results and prior years actual results; and
- an analysis of significant trends relating to the financial information.

8.10 There are a number of sources which can be reviewed with respect to matters of reporting supplementary information beyond that presented in the financial statements. The Public Sector Accounting Board of the Canadian Institute of Chartered Accountants has published general guidance for a government or government organization choosing to provide supplementary information beyond that contained in its financial statements. In addition, most if not all jurisdictions already publish a financial statement discussion and analysis with their Public Accounts.

Recommendation

8.11 A financial statement discussion and analysis should be prepared and accompany the Public Accounts.

Timely Financial Statements

8.12 We continue to stress the importance of releasing the Public Accounts on a timely basis. Financial statements are an important

source of information for decision makers. Their usefulness diminishes as time elapses and increased efforts are needed to have financial statements available on a more timely basis. This is increasingly important with the recent change in the Financial Administration Act regarding years where there is a fixed date for a general election. In the years with a fixed election date, the financial statements for the fiscal year preceding the fixed election date are required to be issued by August 31. The following schedule provides the dates that the Consolidated Financial Statements were released for Canada and the Provinces for the last three years.

CONSOLIDATED (SUMMARY) FINANCIAL STATEMENTS
RELEASE DATES
YEAR ENDED MARCH 31

Jurisdiction	2008	2007	2006
Newfoundland and Labrador	Jan. 30, 2009	Jan. 25, 2008	Dec. 13, 2006
Nova Scotia	Aug. 05, 2008	Aug. 09, 2007	Sept. 29, 2006
Prince Edward Island	Jan. 26, 2009	Jan. 11, 2008	Jan. 31, 2007
New Brunswick	Sept. 26, 2008	Sept. 28, 2007	Aug. 16, 2006
Quebec	Nov. 07, 2008	Dec. 11, 2007	Oct. 24, 2006
Ontario	Aug. 25, 2008	Aug. 17, 2007	Aug 24, 2006
Manitoba	Sept. 24, 2008	Sept. 07, 2007	Sept. 05, 2006
Saskatchewan	June 27, 2008	June 29, 2007	June 29, 2006
Alberta	June 24, 2008	June 21, 2007	June 26, 2006
British Columbia	July 17, 2008	July 11, 2007	July 17, 2006
Canada	Dec. 01, 2008	Oct. 17, 2007	Sept. 28, 2006

8.13 The Financial Administration Act requires each reporting entity to have audited financial statements completed within three months of year end and an annual report available to the public within six months of year end. There are several reporting entities that are not meeting the requirement for audited financial statements and in some cases there were substantial delays in the release of financial statements. When Volume II of the Public Accounts were released on February 19, 2009, an audited financial statement for Harness Racing PEI for the year ended January 31, 2008 and for the Civil Service Superannuation Fund for the year ended March 31, 2008 had not yet been issued.

Recommendation

8.14 Financial Statements should be prepared and released on a timely basis.

Consolidated Budget Estimates

8.15 PSAB Standards set as a basic requirement the inclusion of consolidated budget data with the Public Accounts. Consolidated Budget Estimates were prepared for the first time for the 2003-04 year. To facilitate meaningful comparisons, consolidated budgets need to be prepared and reported on the same basis as that used to prepare the Consolidated Financial Statements. The 2007-08 Budget Estimates were prepared on a consolidated basis but we noted differences in the format used in the Budget and the basis used in the 2007-08 Consolidated Financial Statements. The budget includes the net surplus of Crown Corporations as revenue in the Budget summary. Proper accounting in the Consolidated financial statements requires inclusion of each Consolidated entity's revenues and expenses rather than the net result. The absence of budgeted revenue and expense information of Crown Corporations in budget documents limits the usefulness of budget information in assessing Crown Corporation operations and creates difficulties in comparing budget and financial statement information.

8.16 Although the Province now prepares Capital Estimates, these estimates are not prepared on the same basis as the Province's tangible capital asset policy. Capital budgets include expenditures for assets which are below the threshold limits set by the Province.

Recommendations

8.17 The budget format should be revised to follow the format of the consolidated financial statements of the Province.

8.18 The Province's Tangible Capital Asset Policy should be followed when preparing the budget.

Federal Revenue

8.19 The Province has received significant amounts in federal funding related to a variety of Trust funds established by the Federal Government. The Province records deferred revenue when they initially receive these funds and allocates the funds to revenue over a period of years. We have concerns regarding the accounting treatment applied to the Trust receipts, based on the application of criteria in the PSAB Handbook and inconsistencies with accounting treatment applied to past federal transfers in earlier years where trust agreements were similar. Our research on the issue noted variations among other provincial jurisdictions in accounting treatment for receipts under the Trusts. The area of accounting for government transfers continues to be researched by PSAB.

8.20 As reported over the past several years, we continue to note problems with the timely receipt of amounts due from the federal government. As of December 31, 2008 a Disaster Assistance Claim had yet to be completed relating to the December 2004 Storm Surge. Staff responsible have indicated that a sizable amount of work remains before a claim will be submitted to the federal government. The Office of the Comptroller is reluctant to set up revenue relating to this disaster until a claim is prepared.

8.21 The Public Accounts consolidated statement of financial position reports receivables from the federal government of $64.5 million as at March 31, 2008. Included in this balance is $25 million relating to the Canada-Prince Edward Island Provincial-Territorial Base Funding Agreement. This Agreement was signed September 5, 2008 and provided funding for 2007-08 of $25 million. No monies had been received under this agreement as of December 31, 2008.

8.22 The remaining receivables total $39.5 million. The majority of these receivables will be reimbursed by the federal government on the basis of claims submitted by the Province. Delays in claims submissions result in slower cash flows and higher interest costs to the Province. The following table lists three programs having substantial balances receivable as at March 31, 2008 which were still outstanding at December 31, 2008.

LARGER FEDERAL RECEIVABLES AS AT MARCH 31, 2008 STILL OUTSTANDING AS AT DECEMBER 31, 2008 (Thousands)

	Receivable Mar. 31/08	Cash Receipts Apr.1/08 to Dec. 31/08	Outstanding Dec. 31/08	
Official Languages in Education	$ 7,111	$1,259	$5,852	**Note 1**
Promotion of Official Languages	2,440	-	2,440	**Note 2**
Rehabilitation Programs	1,376	-	1,376	**Note 3**
	$10,927	$1,259	$9,668	

Note 1 FY2006-07: $3,204; FY2007-08: $2,648
Note 2 FY2006-07: $ 877; FY2007-08: $1,563
Note 3 FY2007-08: $1,376

8.23 Discussions with departmental staff indicated that timely submission of claims by the Province is the major factor in delaying receipt of federal contributions.

Recommendation

8.24 All revenues due from the federal government should be claimed and collected on a timely basis.

Tangible Capital Assets

8.25 The Public Sector Accounting Board (PSAB) of the Canadian Institute of Chartered Accountants is responsible for developing generally accepted accounting principles for the public sector. In September 2006, PSAB revised its tangible capital asset standard to disallow the netting of capital revenue against the cost of the related asset. As a result of this change in standards, the Province changed its accounting policy from netting capital revenue against the capital cost to a policy where capital revenue is deferred and amortized over the life of the asset on the same basis as the gross capital cost. The Province has applied this standard retroactively in 2007-08 with restatement of prior periods. Opening tangible capital assets and

deferred capital revenue balances have increased by $64.8 million and current period amortization expense and amortization of deferred capital revenue have increased by $10.3 million as a result of implementing this standard. There has been no change to the surplus (deficit) number.

8.26 The Province's tangible capital asset policy requires capitalization of costs incurred to acquire, construct, develop or better an asset provided it meets the minimum threshold value established for the particular asset. During 2007-08, the Province incurred expenses totalling $2.3 million which were capitalized but were for purchases below the minimum threshold level established for the asset class.

8.27 The Province first began recognizing tangible capital assets in the Public Accounts in 2003-04. That year the Province recognized all tangible capital assets but included an exception with regard to the completeness of land as follows: *"Under the transitional Provisions of PSAB Section PS 3150 historical cost is still being gathered for certain land parcels. Adjustments to cost may be required when more information becomes available."* A similar note is disclosed in the 2007-08 schedule of tangible capital assets. Despite our continued recommendations to address this issue, the Province has not yet determined historical cost for all land parcels.

Recommendations

8.28 The Province's Tangible Capital Asset Policy should be followed when recording capital assets.

8.29 Historical cost information should be obtained for a number of land parcels.

ADDITIONAL FINANCIAL COMMENTS

Outstanding Debentures and Related Accounts

8.30 The largest single liability on the Province's financial statements is its outstanding debentures, which account for $1.31 billion of the Province's $2.08 billion liabilities. All of these debentures have been issued in Canadian dollars. The outstanding debentures can be broken down into public issues of $1.17 billion and Canada Pension Plan issues of $140 million. The public issues have a sinking fund requirement. The Canada Pension Plan issues are for 20 and 30 year periods and do not contain sinking fund requirements.

8.31 During the year the Province redeemed a maturing debenture issue of $35 million. The Province had no new public debenture issues in 2008, opting instead to finance through issuance of short term notes. At March 31, 2008, the Province had outstanding treasury notes in the amount of $125 million. During the year the Province's borrowing rates on treasury notes ranged from 1.90 percent to 4.46 percent.

8.32 At March 31, 2008, the Sinking Fund for debentures held net assets of $266.5 million.

PEI Master Trust

8.33 Investments of the Civil Service Superannuation, Teachers' Superannuation and MLA Pension Funds are consolidated into the Province of PEI Master Trust. Individual funds receive units in the Master Trust based on the net contributions and allocated shares of income and expense. The investments are managed by investment managers external to government and an external custodian is responsible for accounting and record keeping. An Investment Advisory Committee, with representation from government and plan members, provides assistance to Provincial Treasury with the investment of the fund assets. The Fiscal Management Section of Provincial Treasury is responsible for overseeing the Master Trust.

8.34 A revised policy framework for investment of fund assets was developed and approved by Executive Council in September 2006. The revised policy retains asset mix targets of a 65/35 split between equities and fixed income investments and a target of 40 percent investment in non-Canadian equities. The revised policy expands the range of acceptable investments to include investment vehicles such as units of income and real estate investment trusts, foreign debt issues traded on a recognized exchange and mortgage backed securities. Further revisions to the investment policy were approved by Executive Council in December 2007. These revisions provided an investment mandate for a new investment manager and made related adjustments in the mandates of existing managers.

8.35 At March 31, 2008, the pension fund assets as reported by the custodian were $1.220 billion. The following table provides a breakdown of the Master Trust investments as of March 31, 2008 with comparative information at March 31, 2007.

PEI MASTER TRUST
INVESTMENTS
(Millions)

	Year Ended March 31	
	2008	2007
Accrued income	$ 6	$ 5
Short term investments	39	35
Canadian bonds, debentures and notes	445	345
Canadian equity securities	424	466
Foreign equity securities	306	372
	$1,220	$1,223

8.36 The investments include amounts which Master Trust fund managers have invested in their own pooled funds. The March 31, 2008 market values of pooled fund investments total $281 million.

8.37 The market value of the pension plan assets held by the Master Trust was $1.220 billion at March 31, 2008 compared to a market value of $1.223 billion at March 31, 2007. The following table illustrates the components giving rise to the change in assets as well as the rate of return on trust assets.

PEI MASTER TRUST
CHANGE IN TRUST ASSETS
(Millions)

	Year Ended March 31	
	2008	**2007**
Special contributions by Government	$ 34	$ 22
Interest and dividends	48	44
Market value gains/losses	(87)	65
Plan withdrawals and expenses less contributions	(22)	(16)
Transfer of assets from Uniform Pension Plan[1]	24	178
Total increase/decrease	$ (3)	$293
Plan asset rate of return	-3.1%	11.5%

[1] *In prior years health sector employees contributed to the Uniform Pension Plan. This plan was amalgamated with the Civil Service Superannuation Fund.*

8.38 A performance review report prepared by consultants for the Master Trust reported annualized returns of 5.7 percent over a 10 year period to March 31, 2008. Returns for the year ended March 31, 2008 were -3.1 percent while returns reported for the four year period of 2004-2008 were 6.8 percent. Investment returns are a key variable in the magnitude of the unfunded pension obligation. Continuing market declines in 2008 are likely to have a substantial impact on the Province's unfunded pension obligation. Reports from the custodian of the Master Trust reported a market value of $1.056 billion at December 31, 2008.

Pension and Other Benefit Liabilities

8.39 A pension obligation arises when the pension entitlements owed to employees for services rendered exceed pension fund assets. The following schedule shows the total pension liabilities, assets and unamortized expense for the past five years.

	Year Ended March 31 (Millions)				
	2008	2007	2006	2005	2004
Pension fund liabilities	$(1,493.2)	$(1,391.2)	$(1,170.1)	$(1,048.8)	$(1,001.8)
Pension fund assets	1,381.0	1,409.1	1,077.9	831.8	791.1
Unfunded pension (liability) surplus	$ (112.2)	$ 17.9	$ (92.2)	$ (217.0)	$ (210.7)
Unamortized adjustments	155.4	13.6	71.2	49.7	35.1
Net pension assets (obligation)	$ 43.2	$ 31.5	$ (21.0)	$ (167.3)	$ (175.6)

8.40 The above schedule shows a steady increase in the pension liabilities of the various pension plans with fluctuations noted in the market value of plan assets. At March 31, 2007, the market value of plan assets exceeded the estimated pension liabilities by $17.9 million. At March 31, 2008 this situation had reversed and the value of the estimated pension liabilities exceeded the market values of the plan assets by $112.2 million. A net pension asset of $43.2 million was recorded by the Province at March 31, 2008, however, due to unamortized adjustments of $155.4 million.

8.41 Unamortized adjustments arise due to variances between assumptions applied in calculating actuarial estimates and actual results. These variances are initially recorded in the Province's statement of financial position and are amortized over future periods to expense on the Province's statement of operations.

8.42 To reduce the unfunded pension liability, in 2005-06 the Province authorized the issuance of a $160 million note payable to the Teachers' Superannuation Fund and in 2006-07 a similar note was issued to the Civil Service Superannuation Fund in the amount

of $52 million. The notes are payable over ten year periods with interest at 4.345 percent and 4.41 percent.

8.43 During 2006-07 the Uniform Pension Plan (UPP) for Employees of Prince Edward Island Health and Community Services System was amalgamated with the Civil Service Superannuation Fund (CSSF). This resulted in the transfer of $178 million and $24 million in assets in the 2006-07 and 2007-08 years.

8.44 Pension obligations are calculated on an actuarial basis every three years. During the interim period, liabilities are estimated by the Province by extrapolating the data from the most recent valuation. Actuarial valuations were carried out for the Teachers' Superannuation Fund and the Civil Service Superannuation Fund as of April 1, 2005 and for the MLA Pension Funds as of April 1, 2006. The next valuations for the Civil Service Superannuation and Teachers' Superannuation funds will be at April 1, 2008, and the MLA Pension Fund valuation will be at April 1, 2009. As of the date of this report, valuations are in progress for the Civil Service Superannuation Fund and Teachers Superannuation Fund but are not yet completed.

8.45 The following values were reported by the actuary as of the valuation dates:

	(Millions)		
	TSF	**CSSF**	**MLA**
Date of Valuation	**Apr.1/05**	**Apr.1/05**	**Apr.1/06**
Pension fund liabilities	$516.1	$575.8	$15.2
Pension fund assets	308.6	502.0	22.6
Unfunded pension liability	$207.5	$ 73.8	$ (7.4)

8.46 The Province also records liabilities for retirement pay, workers compensation benefits, and death benefits. Note 9(c) of the Consolidated Financial Statements presents a breakdown of other benefit liabilities. The following schedule shows the combined liabilities, assets and unamortized expense relating to retirement pay, workers compensation and death benefits for the past five years.

	Year Ended March 31 (Millions)				
	2008	2007	2006	2005	2004
Other benefit liabilities	$(87.1)	$(78.1)	$(72.9)	$(70.7)	$(67.9)
Fund assets	1.4	1.3	1.3	1.2	1.2
Unfunded liability	$(85.7)	$(76.8)	$(71.6)	$(69.5)	$(66.7)
Unamortized adjustments	3.9	4.5	5.0	1.3	1.4
Net benefit obligation	$(81.8)	$(72.3)	$(66.6)	$(68.2)	$(65.3)

Guaranteed Debt

8.47 The following summarizes the components of the Province's guaranteed debt balances for the past five years as reported on the Guaranteed Debt Schedule.

	Year Ended March 31 (Thousands)				
	2008	2007	2006	2005	2004
Lines of Credit/Demand Loans	$ 2,191	$ 200	$ 1,335	$ 4,128	$ 3,637
Student Loans	25,312	23,897	22,056	19,304	14,029
Debentures/Capital Loans	49,911	52,308	48,857	51,390	50,697
Agencies & Crown Corporations	133,265	94,107	84,313	62,622	33,612
Total Guaranteed Debt	$210,679	$170,512	$156,561	$137,444	$101,975

8.48 There has been a significant increase in the value of guarantees issued by the Province over the past five years. Included under Agencies and Crown Corporations are guarantees of Island Investment Development Inc's Century 2000 Fund notes payable to the Minister of Citizenship and Immigration. At March 31, 2004 the value of these notes was $19.8 million compared to $127.5 million at March 31, 2008, a significant four year increase of $107.7 million. Student loan guarantees also increased significantly over this period, from $14 million at March 31, 2004 to $25.3 million at March 31, 2008.

8.49 The Province has included provisions for losses of $4.6 million on the loan guarantees and provisions totalling $16.6 million relating to other guarantees described in notes 7(i) and 8(b) of the Public Accounts. Schedule 21 of the Public Accounts shows a continuity schedule for the Provision for Doubtful Accounts.

8.50 In addition to the guaranteed debt balances noted above, notes 7(i), 8(b) and 8(c) to the Consolidated Financial Statements provide information on three additional guarantees. These guarantees have been disclosed in the Public Accounts notes but have not been included on the Guaranteed Debt Schedule in the Public Accounts. Note 7(i) relates to arrangements with Charlottetown Area Development Corporation in relation to costs of properties purchased from Canadian National Railway in 1996. Note 8(b) indicates the PEI Business Development Inc. has indemnified lease payments to a landlord on behalf of a private company. In the case of default by the tenant, the maximum amount indemnified is $108,000 per month, pursuant to the lease ending February 2025. Note 8(c) provides information on the guarantee to the Credit Union Deposit Insurance Corporation. Based on unaudited information, Prince Edward Island Credit Unions held insurable deposits of $482.5 million at September 30, 2007.

Cancellation or Discharge of Debt

8.51 Section 16 of the Audit Act requires the Auditor General to report the total amount of any claims, debts or monies due to the Province that have been discharged, cancelled, and released under Section 26 of the Financial Administration Act. In 2007-08, the amount cancelled or discharged under Section 26 totalled $677,116 and the amount written off under Section 26.1 was $1,315,830 as follows:

	Section 26(1)	Section 26.1(1)
Revenue Tax Act	$ -	$ 599,350
Environment Tax Act	-	2,760
Real Property Tax Act	83,635	-
Social Assistance Act	579,957	-
Department of Health	-	678,225
P.E.I. Agricultural Insurance Corp.	13,524	35,495
	$677,116	$1,315,830

8.52 The total amount discharged, cancelled and released or written off owed by third parties to the Province was $1,992,946.

Surplus (Deficit) of Crown Agencies and Corporations

8.53 Section 16 of the Audit Act requires the Auditor General to include information in the Annual Report on deficits of agencies not covered by appropriations in the year in which they have been incurred, and any surpluses not paid into the Operating Fund in the year in which they are earned. For information purposes we have also included the cumulative surplus or deficit for each entity.

	Annual Surplus (Deficit) For the Year	Cumulative Surplus (Deficit)
AGENCY		
Advisory Council on the Status of Women	$ (24)	$ (4,523)
Agricultural Insurance Corporation	980,307	16,123,646
Agricultural Research Investment Fund Inc.	12,775	146,876
Aquaculture and Fisheries Research Initiative Inc.	8,399	706,980
Business Development Inc.	117,225	1,715,812
Charlottetown Area Development Corporation	19,451	5,036,823
Eastern School District	179	4,072
Energy Corporation	3,182,140	7,428,531
French Language School Board	9,169	13,420
Grain Elevators Corporation	109,106	635,309
Human Rights Commission	11,179	-
Island Investment Development Inc.	2,328,666	2,808,009
Island Waste Management Corporation	1,410,484	154,199
Lending Agency	603,988	244,862
Museum and Heritage Foundation	(29,588)	582,706
Self-Insurance and Risk Management Fund	78,166	7,528,273
Special Projects Fund	(92,060)	642,211
Summerside Regional Development Corporation Ltd.	236,851	3,533,062
Tourism P.E.I.	3,516,563	-
Western School Board	364,153	370,654
Workers Compensation Board	291,107	12,237,850

8.54 Audited financial statements for Harness Racing PEI for the fiscal year ended of January 31, 2008 were not completed at the time the listing was prepared.

MANAGEMENT RESPONSE

8.55 These matters have been discussed with Management.

9. APPROPRIATIONS

INTRODUCTION

9.1 Our audit of Appropriations for the year ended March 31, 2008 included a review of the systems and procedures for the administration of the Province's annual budget. This required an audit of appropriations approved by the Legislature and special warrants approved by Executive Council on the recommendation of Treasury Board.

9.2 The Appropriation Acts provide the spending authority for government and are approved by the Legislative Assembly annually. Appropriations for 2007-08 were approved in the Appropriation Act (Current Expenditures) 2007 and Appropriation Act (Capital Expenditures) 2007. If additional funds are required during the year, special warrants are issued by the Lieutenant Governor in Council.

9.3 In **SCHEDULE A** attached to this report, we provide a comparison of appropriations to actual expenditures in accordance with the classifications in the Appropriation Acts 2007.

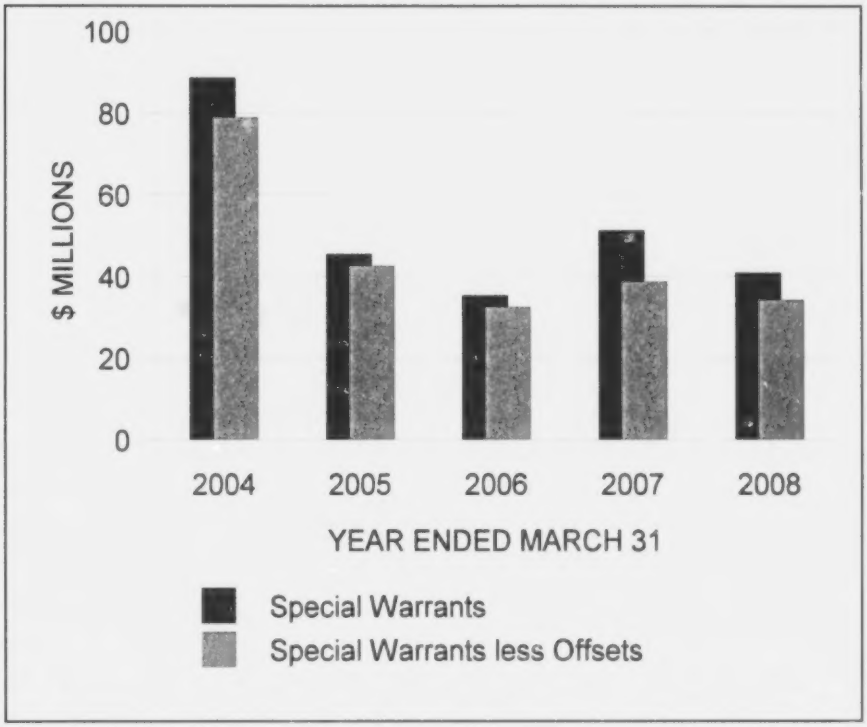
SPECIAL WARRANTS

9.4 Section 16(h) of the Audit Act requires the Auditor General to list in detail appropriations made by special warrant and the purpose of such appropriations. Details are shown in **SCHEDULE B** attached to this report.

9.5 For the 2007-08 fiscal year, special warrants totalled $40.9 million compared to $51.3 million in 2006-07. Of the special warrants issued for 2007-08, $6.7 million were offset by revenue. The result was a net increase in provincial appropriations of $34.2 million.

9.6 **Exhibit 9.1** indicates the gross special warrants and special warrants net of any offsets for the last five years.

EXHIBIT 9.1
SPECIAL WARRANTS



Delay in Issuing Special Warrants

9.7 Normally an expenditure should not be incurred unless it is provided for by an appropriation. At year end, adjustments may be necessary to ensure the financial statements present fairly the revenue and expense of the Province. When this occurs, it would be expected that a special warrant would be issued on a timely basis for any overexpenditures.

9.8 During our audit for the year ending March 31, 2008, we noted two departments had overexpenditures in their capital accounts, and one in its ordinary account with no special warrants issued until March 3, 2009.

Recommendation

9.9 Special warrants should be issued on a timely basis.

Capital Expenditures

9.10 In December 2006, an Appropriation Act (Capital Expenditures) 2007 was passed, which included appropriations for expenditures to be made for capital items. It would be expected that capital and current expenditures would be budgeted in accordance with the tangible capital asset policy.

9.11 During our audit, we noted cases where the Tangible Capital Asset Policy was not followed. Six departments had vehicles that were capitalized however, they were budgeted and expended in their current accounts.

9.12 We realize this is only the second year for a capital Appropriation Act and expect differences such as the above will be addressed in future years.

Recommendation

9.13 The tangible capital asset policy should be taken into consideration when preparing the Appropriation Acts for current and capital expenditures.

MANAGEMENT RESPONSE

9.14 We have discussed our findings with management.

UPDATE ON PREVIOUS RECOMMENDATIONS

10. UPDATE ON PREVIOUS RECOMMENDATIONS

INTRODUCTION

10.1 Each special audit results in a report which is provided, through our annual report, to the Legislature. A fundamental component of special audit reports are recommendations which address observations or deficiencies noted during the audit. They are designed to contribute to the improvement of the management and administration of government operations and programs. It is management's prerogative to select the best course of action to address the problems identified. Our concern is that all recommendations are being addressed by management.

10.2 Annually we request information on the action taken in addressing outstanding recommendations. This information is normally requested through the Deputy Minister or Chief Executive Officer of the organization. At a minimum, we review each response for reasonableness. It is normally more cost effective to do detailed verification during the next scheduled audit.

10.3 Following is summary information provided to us on the status of recommendations from the special audits and examinations reported in the 2008 Annual Report of the Auditor General as well as outstanding recommendations from audits in the 2007, 2006, and 2004 Annual Reports.

MEDICAL EQUIPMENT - ACQUISITION AND MAINTENANCE

10.4 Following are the recommendations resulting from our audit of Medical Equipment - Acquisition and Maintenance as presented in the 2008 Annual Report of the Auditor General. The status of implementation of the recommendations is provided based on information received from management of the Department of Health.

Auditor General's Recommendation	Status/Management Response
In cooperation with Queen Elizabeth Hospital and Prince County Hospital, the Department of Health should develop a five-year medical equipment capital plan.	Hospital administrations from both Queen Elizabeth Hospital and Prince County Hospital, as well as community hospitals and other sites, have provided the Department of Health with their annual capital requirements to be incorporated into the Department of Health five year capital budget. While some sites have provided a five-year plan, not all sites have been able to accomplish this for the 2009-10 capital submission. It would be our intention to have all sites provide a five-year plan which will be co-ordinated by the Department of Health.
The Department of Health should use a medical equipment capital plan to support requests for funding through government's budgeting process.	Requests for medical equipment were included in the 2009-10 capital budget process to the extent they were not funded by the foundations. The intention for the 2010-11 capital budget request is to include all required equipment with a revenue offset for funding provided by the respective foundations.
To assist in ranking equipment priorities, the items on the Queen Elizabeth Hospital medical equipment priorities listing should be supported with a documented needs assessment.	The QEH is in the process of developing a priority needs assessment process similar to what now exists at the PCH site.

Auditor General's Recommendation	Status/Management Response
Any changes to the approved medical equipment priorities lists should be re-submitted to the committee for approval.	This recommendation has been implemented.
Policies should be developed and approved by the Department of Health regarding the circumstances required for standardization of medical equipment.	Since restructuring in 2005, there have been great strides made in the standardization of equipment and supplies. A number of joint committees have been established with membership from both acute sites to look at areas where standard equipment can be procured. There are a number of criteria considered in the selection of products including compatibility with existing equipment; issues with using multiple types of same purpose machines; and training and safety issues with switching manufacturers, especially in surgical and operating room areas. However, there is a need to have policies consolidated and documented.
Medical equipment which is no longer used at one hospital but is still safe should be transferred to another hospital where it can be used.	While this area has limited potential as most equipment being replaced is not suitable for other use, equipment will be shared with other possible sites where it is appropriate and safe.
The bid evaluation for major pieces of medical equipment should be well documented and maintained to support the vendor selection.	This information will be retained in the future.
Procurement procedures should be fair and open to all bidders and, where applicable, should comply with the requirements of the Agreement on Internal Trade.	This recommendation is being followed. Only in exceptional circumstances, such as safety of use and connectivity to other complex equipment, will items not follow the strict rules of procurement.

Auditor General's Recommendation	Status/Management Response
For major medical equipment purchases, where a lease option is available, any decision regarding lease versus buy should be supported with a documented analysis.	Where leasing is an option, it will be considered and documented and analysis will be retained regarding a decision as to buy or lease.
Delegation of signing authority should be supported with documented approval.	This recommendation is being followed.
Purchase orders and payments should be approved by persons with appropriate signing authority.	This recommendation is being followed.
The Department of Health should follow the Public Purchasing Act Regulations and Treasury Board Policy on the Delegation of Signing Authorities. Where changes are considered appropriate, the Department should seek approval of Executive Council or Treasury Board as applicable.	This recommendation is being followed.
A complete database of medical equipment should be maintained at both the Queen Elizabeth Hospital and the Prince County Hospital.	As a result of our voluntary participation in a national accreditation process and based on recommendations from the Auditor General's report, a Preventative Maintenance Sub-Committee of the Environmental Accreditation Team was formed to deal with some of the recommendations coming from both those reports. The goals of this committee are to establish standards and controls, create and maintain inventories, establish priority categories for equipment based on risk and to develop policies and procedures to begin introduction of these processes in all our health facilities.

Auditor General's Recommendation	Status/Management Response
	On June 3, 2008 Senior Management agreed to fund a preventative maintenance program, including the purchase of asset management software. The software system will be used for all medical and non-medical equipment and it will provide the capability of entering work order data, preventative maintenance scheduling, and procedures, as well as record keeping. The asset management software has been purchased and is in the process of being implemented province wide.
The Queen Elizabeth Hospital and Prince County Hospital should have documented policies for preventative maintenance of medical equipment and a process in place to flag equipment when preventative maintenance is due.	One of the goals of the Preventative Maintenance Committee will be to continue to work on documenting policies for preventative maintenance. The new asset management software will have the ability to flag equipment for preventative maintenance.
Maintenance systems for medical equipment should record all repairs and preventative maintenance completed and should be used to provide periodic reports to senior management.	The purchase of the asset management software will improve the management of repairs and preventative maintenance. A periodic reporting to senior management will be developed.
Planned and unplanned downtime for major medical equipment should be recorded to monitor whether operating performance uptime guarantees have been breached.	The preventative maintenance scheduling within the asset management software, will allow scheduled down times to be recorded. The system will assist in organizing the proper time for maintenance, and will provide an analytical tool to review outcomes of the planned downtime.

Auditor General's Recommendation	Status/Management Response
The Department of Health should re-examine biomedical services to determine the most cost effective method to manage the risks associated with the operation and maintenance of medical equipment.	During the summer of 2008, the Department commissioned an expert biomedical consultant from Nova Scotia to conduct a review of bio-medical services for the Department of Health. The report was received by the Department on November 14, 2008 and includes a number of recommendations which the Department is presently reviewing.

MANAGEMENT AND USE OF DIAGNOSTIC IMAGING EQUIPMENT

10.5 Following are the recommendations resulting from our audit of Management and Use of Diagnostic Imaging Equipment as presented in the 2008 Annual Report of the Auditor General. The status of implementation of the recommendations is provided based on information received from management of the Department of Health.

Auditor General's Recommendation	Status/Management Response
The Department of Health in cooperation with Diagnostic Imaging Services should work to ensure that the definition of levels of priority and wait time targets are consistent.	Through working with the PEI Wait Times Strategy Committee since March 2008, definitions of priority wait times targets for Diagnostic Imaging (DI) have been revised to reflect national benchmark definitions of: emergent, urgency I (P1), urgency II (P2), urgency III (P3). The P4 category has been eliminated.
Current information should be publicly available on wait times for CT and MRI scans.	Currently, 2006-07 wait time information can be found at: http://www.gov.pe.ca/health/. There will be a new web page launched in early 2009 that will provide quarterly wait time data and other relevant information.
Referrals for CT diagnostic testing should be recorded in the Radiography Information System when received.	Changes to the Radiology Information System now allow the time of receipt of the referral at Diagnostic Imaging to be captured. A process has been implemented so all requests for DI exams are now entered into the queue immediately upon delivery to DI. The process was developed to capture actual wait times as described in the provincial wait times strategy and measures the time from request into DI to the time the exam is completed.

Auditor General's Recommendation	Status/Management Response
The method for calculating and reporting wait times for diagnostic imaging should be improved. Wait times should be reported in accordance with the PEI Wait Time Strategy and should be substantiated with data from the Radiography Information System.	Once the PEI Wait Times Strategy committee steering committee was formed and met in March 2008, DI definitions of priority and wait time targets were changed to reflect common national benchmarks. Reports of DI wait times are shared with the Provincial Wait Time Coordinator on a monthly basis.
In accordance with the PEI Wait Time Strategy, the Department of Health should ensure that all patients are scheduled for diagnostic imaging tests based on prioritized medical need.	All patients are booked based on medical needs as follows: Emergency; Urgent I (P1); Urgent II (P2) semi-urgent; Urgent III (P3) - elective/routine outpatients. Exams are reported based on priority: Emergent, Inpatients, urgent (all images and modalities), followed by MRI, CT, Ultrasound, Nuclear Medicine, Diagnostic Breast Imaging, General Imaging, BMD (Bone Mineral Densitometry) and Breast Screening. Outside operational hours, similar to other Canadian jurisdictions, MRI may be utilized for research and/or WCB patients.

Auditor General's Recommendation	Status/Management Response
The Department of Health should increase efforts to recruit additional radiologists. The Department should examine other options to meet demand such as transferring diagnostic images to radiologists off Island.	Diagnostic Imaging along with the Recruitment and Retention Secretariat have increased efforts to support recruitment. A recruitment DVD has been created in order to provide presentations to potential candidates in medical schools in particular, in Atlantic Canada. This will also be made available on the Department of Health website for prospective candidates. Locums are utilized whenever possible to support the full time radiologists. A teleradiology pilot project will be launched January 2009 and will evaluate transmitting images off Island to Nova Scotia.
Recruitment for ultrasound sonographers should be addressed to improve the wait times for ultrasound tests.	Efforts to recruit and retain ultra-sonographers have been implemented: return-in-service agreements have been reviewed and improved. As a result, DI hired one FTE at the QEH in September 2008; an additional ultrasonographer will complete her studies and begin working at PCH August 2009 and one additional candidate is pending for September 2009 at the QEH. A proposed wage increase to improve competitive advantage has been approved and settled. This improves recruitment as well as retention of existing employees. Where possible, off-Island temporary/casual ultrasonographers are utilized. This part-time support is an ongoing and successful short term initiative.

Auditor General's Recommendation	Status/Management Response
Targets for turnaround times for CT, MRI and ultrasound tests should be developed.	Turnaround time is defined as the time that an exam is completed to the time the report is generated. This is dependent upon the availability of radiologists to interpret the exams as well as transcriptionists to type the exam reports. While few national benchmarks exist, the exams are prioritized with the most critical patient reports (emergencies and inpatients) reported and transcribed within 24-48 hours. Once exams are reported, they are available on the dictaphone system for referring physicians to listen to. Referring physicians can also, at any time, consult with an onsite radiologist. Once a more complete complement of radiologists is available, a more consistent approach to targets will be implemented.
The quality control coordinator should ensure that turnaround times are monitored and unusual delays followed up.	This position is responsible for monitoring wait times as well as report times. These are reported to the provincial wait times coordinator on a monthly basis, as well as the DI Director on a weekly basis. Any outstanding reports are followed up as are public and physician requests.

Auditor General's Recommendation	Status/Management Response
Diagnostic Imaging Services should implement a quality assurance program that includes a peer review of a sample of each radiologist's analysis of diagnostic images.	A peer review program for radiologists is currently not standard practice across Canada; however, DI is evaluating potential benchmarks with other jurisdictions. Internally, all locums and new radiologists have report samples reviewed on a random basis. It is standard practice for the radiologists to consult with each other on complex cases; any questionable reports are discussed as a group on an ad-hoc basis. With the significant shortage of radiologists available to interpret exams, a more formalized audit program, at this time, would further increase wait times and turnaround times due to the additional workload.
The Department of Health in cooperation with the hospitals should review the utilization of MRI and CT equipment.	Utilization of DI equipment is dependent upon number of radiologists and the appointment booking schedule is a reflection of radiologist availability. With the Teleradiology project slated to begin January 2009, operational hours for CT and MRI will be extended. Additional positions for CT at both QEH and PCH have been approved and are in place. MRI exams have already been expedited and the number of bookings per day had been increased. This had reduced the wait times for MRI specific exams by 50 percent, from 6-7 months to 3-5 months.

Auditor General's Recommendation	Status/Management Response
Diagnostic Imaging Services should consider implementing a centralized booking process for the two CT scanners, at QEH and PCH.	DI utilizes centralized booking processes for ultrasound and breast screening. In order to implement central booking for CT scans, changes to the electronic scheduling templates are required. In addition, operational hours in both sites for CT scans will be extended to accommodate additional appointments which should reduce overall wait times.
Planned and unplanned downtime of major diagnostic equipment should be monitored and reported to senior management.	The Biomedical service supports and controls all service aspects of DI equipment including vendor support. Preventative maintenance is to be scheduled by Biomedical with DI supervisors. Downtime documentation is created and copies will be kept in the respective DI rooms. Biomedical will set up a process to more closely track downtime but due to resources, this is not yet available at the QEH.

Auditor General's Recommendation	Status/Management Response
The Department of Health should make increased efforts to inform both physicians and patients on the radiation exposure from CT scans.	In 2004, a letter from the Medical Director of the Provincial Health Services Agency was sent to all medical staff. It described radiation doses from a variety of exams, including CT scans and encouraged discretion in ordering CT scans. The letter also recommended a review of the booklet, "Making the Best Use of Clinical Radiology." By accessing a link from the PEI DOH/QEH website, http://www.radiologyinfo.ca, the public and physicians can access the direct link to the CAR (Canadian Association of Radiologists) website. This offers information on exam descriptions and radiation doses, including CT scans.
The radiation dose levels for pediatric patients should be reviewed and monitored to ensure the radiation exposure is as low as reasonably achievable.	DI has created an electronic template and database of pediatric CT scans from 2002 to 2008, which records the radiation dose of pediatric patients. In addition, the DI Medical Physicist has utilized, "Image Gently," a website created by the Alliance for radiation safety in pediatric imaging, with specific processes on "How to develop CT Protocols for Children." http://www.pedrad.org/associations/5364/ig/

Auditor General's Recommendation	Status/Management Response
A database should be maintained on individuals who have multiple CT scans. This information should include accumulated radiation exposure and should be accessible for consideration in clinical evaluations.	Many oncology patients have multiple CT scans for treatment planning and evaluation of disease progression. The DI Medical Physicist has tracked the most commonly occurring CT exams - CT KUB (abdomen CT). Those patients are now tracked and as a result, DI has implemented a "low dose" protocol for those patients having CT KUBs.
Diagnostic Imaging Services should implement a quality assurance program for both the MRI and CT scanners.	The MRI coordinator will attend a U.S. program in February 2009 in order to establish an appropriate Quality Assurance (QA) program for MRI. To support this program, MRI physician and patient education is available on the PEI Department of Health website. A QA program has been implemented for CT scans with daily, weekly, monthly, quarterly and annual quality system evaluations and tests performed on the CT scanners at QEH and PCH. Audits on radiation doses from CT scans are also performed as part of the QA program.

TRAVEL - GOVERNMENT DEPARTMENTS

10.6 Following are the recommendations resulting from our audit of Travel - Government Departments as presented in the 2008 Annual Report of the Auditor General. The status of implementation of the recommendations is provided based on information received from the Secretary to Treasury Board.

Auditor General's Recommendation	Status/Management Response
Treasury Board policy regarding personal travel to and from a work location should be complied with. Any exceptions to Treasury Board policy should receive Treasury Board approval.	Any exceptions to Treasury Board policy require Treasury Board approval.
In accordance with the UPSE Collective Agreement and Treasury Board policy, departments should review, on an annual basis, employees' continued eligibility for a monthly travel allowance.	All employees in eligible classifications will be required to apply for the low distance allowance every twelve months. Departments in consultation with Public Service Commission will determine eligibility based on requirements of the Collective Agreement and Treasury Board policy.
Departments should implement controls to cross reference PCard travel transactions with travel claims to ensure transactions paid by using a PCard are not claimed for reimbursement by the employee.	Departmental administrators have been advised to review PCard activity on the Province's financial information system before approving travel claims.
The PCard Policy and Procedures document should be amended to more clearly outline PCard usage and the responsibilities for program administration.	The PCard Policy is being reviewed by the Office of the Comptroller to ensure responsibility for program administration is clarified.
As approved by Treasury Board, PCard policies should be included in the Treasury Board Policy and Procedures Manual.	Following the review by the Comptroller's office, the PCard policy will be included in the Treasury Board Policy and Procedures Manual.

Auditor General's Recommendation	Status/Management Response
In accordance with PCard policies, departments should ensure that all PCard logs are prepared, approved and submitted to the Office of the Comptroller.	The Office of the Comptroller has established a process for collecting PCard logs which will be reviewed for proper preparation and approval.
In accordance with Treasury Board policy, departments should complete a documented cost benefit analysis on options to meet their annual travel needs.	Treasury Board staff are reviewing the Treasury Board policy for Government Vehicles. When the review is complete, the revised policy will be approved by Treasury Board and communicated to departments and reporting entities.
Departments should ensure that Treasury Board policy regarding assignment of government vehicles is complied with.	Treasury Board staff are reviewing the Treasury Board policy for Government Vehicles. When the review is complete, the revised policy will be approved by Treasury Board and communicated to departments and reporting entities.
Treasury Board should re-examine the distance thresholds outlined in its travel policy.	Treasury Board staff will be reviewing distance thresholds as part of its review of Treasury Board policy on Government Vehicles.
Departments should ensure that employees, who are assigned a government vehicle or given primary responsibility for a pool vehicle, sign the prescribed Treasury Board vehicle acknowledgement forms.	The requirements of Treasury Board policy regarding vehicle aknowledgement forms were reviewed with the departments of Health and Social Services and Seniors.
Departments should ensure compliance with the Treasury Board policy requirement to make payment for personal use of government vehicles, and take immediate action to collect all amounts due from employees.	Treasury Board staff are reviewing the Treasury Board policy for Government Vehicles. When the review is complete, the revised policy will be approved by Treasury Board and communicated to departments and reporting entities.

10. Update on Previous Recommendations

Auditor General's Recommendation	Status/Management Response
Departments should ensure that monthly log reports are prepared and submitted on a timely basis.	The requirement for monthly logs was reviewed with senior management of the departments involved.
In accordance with Treasury Board policy, departments should ensure that credit card acknowledgment forms are signed when employees are issued fleet credit cards.	Treasury Board staff are reviewing the Treasury Board policy for Government Vehicles. When the review is complete, the revised policy will be approved by Treasury Board and communicated to departments and reporting entities.
In accordance with Treasury Board policy, Procurement Services of Provincial Treasury should maintain a master list of all fleet credit cards issued.	Procurement Services is maintaining a master list of all credit cards issued.
Departments should ensure that an accurate up-to-date list is maintained of all fleet credit cards issued, and only one card should be issued for each vehicle.	Treasury Board staff are reviewing the Treasury Board policy for Government Vehicles. When the review is complete, the revised policy will be approved by Treasury Board and communicated to departments and reporting entities.
The Department of Transportation and Public works should implement procedures to verify fleet credit card billings.	The Department has implemented the necessary procedures to ensure credit card billings are correct.
Service vehicles in the Department of Transportation and Public Works should be added to the corporate fleet listing, and any operating costs of these vehicles, paid for with fleet credit cards, should be allocated to specific vehicles.	The Department is in the process of adding service vehicles to the corporate fleet listing.

Auditor General's Recommendation	Status/Management Response
Departments should ensure that listings of government vehicles on the Fleet Management System are complete and accurate and vehicle usage and operating costs are entered on the Fleet Management System.	Treasury Board staff are reviewing the Treasury Board policy for Government Vehicles. When the review is complete, the revised policy will be approved by Treasury Board and communicated to departments and reporting entities.

SMALL CLAIMS PROCESS

10.7 Following are the recommendations resulting from our audit of the Small Claims Process as presented in the 2008 Annual Report of the Auditor General. The status of implementation of the recommendations is provided based on information received from management of the Office of the Attorney General.

Auditor General's Recommendation	Status/Management Response
An information brochure should be developed and available which describes the requirements of the Small Claims process and the limitations on collection.	The brochure is in its final stages of preparation and should be available to the public in fiscal 2009-10.
Documented targets should be established for the timely processing of Small Claims cases and actual results measured against the targets.	Small Claims Section has established documented targets in defended actions and actual results are now being measured against the targets.
The current practice for scheduling cases for trial should be re-examined.	This recommendation pertains to judicial administration, which is within the exclusive jurisdiction of the Judiciary, and therefore beyond the authority of the Office of the Attorney General.
Action should be taken to ensure that a management information system is in place which provides sufficient, appropriate information for planning and decision making for the Small Claims section.	Process changes have been undertaken to ensure that our case tracking system provides sufficient and appropriate information for planning and decision-making for the Small Claims Section.
The Prothonotary's Office should ensure that all writs are filed with Sheriff Services for collection as soon as they are registered.	This has been implemented in the Small Claims Section.

Auditor General's Recommendation	Status/Management Response
Sheriff Services should establish a checklist of collection procedures. Documentation on the completion of the procedures should be maintained for each case.	This has been implemented.
The commission for Sheriff Services should be consistently calculated	This has been implemented.
Sheriff Services should, where possible, access government managed information systems such as the Motor Vehicle Registration system and the Property Tax system to determine if debtors hold assets which can be seized. Reviewing these databases should be part of the procedures required for writ collection.	The primary responsibility for identifying property of the debtor lies with the creditor. Any research undertaken by Sheriff Services is to assist the creditor and not part of the duties of Sheriff Services.
Information available to Sheriff Services should be improved to provide a Province-wide list of outstanding writs and to allow for enhanced management of writ collection activities.	The Charlottetown Sheriff's office maintains a list for Kings County and Queens County. The Summerside Sheriff's office maintains a list for Prince County.
Performance measures should be established for court services and the Legal and Judicial Services Division should report to senior management and the Legislature on the performance of court services including Small Claims.	This recommendation, because of its constitutional implications, requires in-depth consideration by legal officers in the Office of the Attorney General and will be responded to in due course.

PROPERTY TAXATION

10.8 Following are the outstanding recommendations resulting from our audit of Property Taxation as presented in the 2007 Annual Report of the Auditor General. The status of implementation of the recommendations is provided based on information received from management of the Taxation and Property Records Division of the Department of the Provincial Treasury.

Auditor General's Recommendation	Status/Management Response
Criteria should be developed and documented for flagging property transfers that require additional verification to substantiate compliance with the Real Property Transfer Tax Act.	Procedures have been developed and implemented. The Registrar of Deeds flags newly registered accounts in situations where the Registry Office has determined that additional information is required to verify compliance with the Real Property Transfer Tax Act. Procedures include flagging all accounts where a current assessment is not available, transactions involving family members where the Registrar questions the family relationship and/or other transactions where the Registrar feels further verification is required.
Division management should continue to take action to ensure all outstanding system components and reporting capabilities are developed and provided by the system developer.	Core system components and reporting capabilities have been developed and provided by the system developer. Significant work on modules including automated depreciation and CAMA system for valuation, analysis and quality control of residential and recreational properties was completed in 2008 in preparation for 2009 assessment year implementation. System maintenance and enhanced reporting requests will be ongoing for the life of the system.

Auditor General's Recommendation	Status/Management Response
Division management should review user access to ensure that access approved provides adequate segregation of incompatible functions, and is limited to essential access related to job responsibilities.	A user profile list has been requested from Information Technology Shared Services (ITSS). This list will be reviewed and, if applicable, user access profile changes will be completed by March 31, 2009.
The Division should reconcile partial billings to the accounts receivable postings and tax bills mailed.	Procedures for reconciliation of partial billings to the accounts receivable postings have been developed and implemented. Reconciliation of partial billings to the number of tax bills mailed remains outstanding. Mail transaction audit functionality will be required from within the Queen's Printer. The value of such reconciliation is recognized. Best efforts will be made to communicate requirements and facilitate the availability of mail reconciliation information from Queen's Printer by June 30, 2009.

Auditor General's Recommendation	Status/Management Response
The Property Tax Section should establish a disaster recovery plan which sets out the requirements to re-establish the property tax system in the event of a disaster. The disaster recovery plan should be tested periodically to ensure it is operational.	Operating procedures in support of system recovery are the responsibility of Information Technology Shared Services (ITSS). In the event of system failure, the Taxation and Property Records Division would depend on ITSS to implement recovery procedures which would ensure system availability within a reasonable period of time. Review and endorsement of recovery procedures and recovery time objectives will take place as part of annual information technology business plan processes for 2009-10. Work on developing business continuity plans for each section of the Taxation and Property Records Division will be prioritized early in 2009 and extend over a 1 to 2 year period and result in a business continuity program for the Division. Business continuity programs mandate ongoing plan update and testing. Significant resources from within the Division and from ITSS will be required. Required resources and participation by ITSS will be identified as a divisional IT Business Plan priority for 2009-10. In the end, time lines will largely depend on the availability of such resources.

PEI ENERGY CORPORATION

10.9 Following are the outstanding recommendations resulting from our examination of the PEI Energy Corporation as presented in the 2007 Annual Report of the Auditor General. The status of implementation of the recommendations is provided based on information received from management of the PEI Energy Corporation.

Auditor General's Recommendation	Status/Management Response
The Energy Corporation should develop a strategic plan that is linked to the renewable energy strategy and approved by the Board of Directors.	In October 2008, the Government released a wind development strategy entitled Island Wind Energy Securing our Future: The 10 Point Plan. This was followed up by the release in November of the Department's energy strategy entitled Prince Edward Island Energy Strategy Securing our Future: Energy, Conservation and Renewables. Both strategic planning documents have identified roles for the PEI Energy Corporation pertaining to the further development of domestic wind energy and the implementation of a Request for Proposal process for the development of export wind capacity. The Corporation is in the process of developing a more detailed strategic plan for the development of the renewable technologies discussed in these documents. Board of Directors approval on the plan will be sought prior to mid 2009.

10. Update on Previous Recommendations

Auditor General's Recommendation	Status/Management Response
The Energy Corporation should prepare a business plan, linked to its strategic plan, that outlines planned activities and required resources.	The Corporation is currently developing a business plan to complement the proposed strategic plan. It is the intention of the Corporation to seek approval from the Board of Directors for the business plan at the same time as the strategic plan is being considered. Board approval will be sought prior to mid 2009.

WORKFORCE INCENTIVE PROGRAMS

10.10 Following is an outstanding recommendation resulting from our audit of Workforce Incentive Programs as presented in the 2007 Annual Report of the Auditor General. The status of implementation of the recommendation is provided based on information received from management of the PEI Public Service Commission.

Auditor General's Recommendation	Status/Management Response
The Public Service Commission should prepare a final report on the Workforce Renewal Program including the impact on the size of the public service, the direct costs and estimated savings. The report should be provided to Executive Council.	The Public Service Commission prepared a final report on the Workforce Renewal Program including the impact on the size of the public service, the direct costs and estimated savings. Executive Council acknowledged receipt of the final report at its meeting on October 7, 2008.

PEI BUSINESS DEVELOPMENT INC. - LENDING ACTIVITIES

10.11 Following are the outstanding recommendations resulting from our examination of PEI Business Development Inc. - Lending Activities as presented in the 2007 Annual Report of the Auditor General. The status of implementation of the recommendations is provided based on information received from management of PEI Business Development Inc.

Auditor General's Recommendation	Status/Management Response
The draft policy manual for lending activities should be revised where necessary and approved.	Legislation has been given Royal Assent that will replace PEI Business Development with Innovation PEI. Once the Act is in place and Innovation PEI's new Board is formed we will review with and seek the input of the Board prior to implementing any updated policies.
The decision making authority of the Lending Board within BDI should be clarified under the PEI Business Development Inc. Act Regulations.	Regulations are being prepared which will clearly define the role of the Board as it relates to Lending under the Innovation PEI Act.
In accordance with guidance provided by Citizenship and Immigration Canada, funds should not be advanced to provincial organizations from the PEI Century 2000 Fund Inc. to be used for private sector investment.	Funds of PEI Century 2000 Fund Inc. are no longer being advanced to provincial organizations.

STUDENT TRANSPORTATION - EASTERN SCHOOL DISTRICT

10.12 Following is an outstanding recommendation resulting from our examination of Student Transportation-Eastern School District as originally presented in the 2006 Annual Report of the Auditor General. The status of implementation of the recommendation is provided based on information received from management of the Eastern School District.

Auditor General's Recommendation	Status/Management Response
In accordance with Eastern School District policy, a standard performance appraisal process should be implemented for bus drivers.	The Eastern School District has been working on a performance appraisal process for bus drivers. There have been some unforeseen challenges and the District is not ready to fully implement the process.

EAST PRINCE HEALTH - SENIORS SERVICES

10.13 Following are the outstanding recommendations resulting from the audit of East Prince Health-Seniors Services as presented in the Auditor General's 2006 Annual Report to the Legislative Assembly. The status of the implementation of these recommendations is presented based on information received from management of the Department of Health.

Auditor General's Recommendation	Status/Management Response
A workload measurement standard should be developed which defines minimum levels of care for residents of nursing homes. The standard should be supported by a breakdown of the extent of care to be provided by nursing staff and other staff. Staffing budgets should be established to meet this standard.	The Department has approval to replace Prince Edward Home and Summerset Manor as Phase I of the Government's manor replacement strategy. Currently, the Department is in the functional planning stage. Within the scope of functional planning is the development of an appropriate staffing model to deliver optimal level of care to nursing home residents. The functional planning recommendations are expected by April 2009. The Department will review these recommendations with the aim to develop a standard for appropriate staffing in all public manors.
The Department of Health should investigate the feasibility of computerization to reduce the duplicate manual entries required in staff scheduling.	The Department of Health is in the process of developing a business plan with ITSS to cost out electronic central staff scheduling. The intent would be to minimize the effort required to schedule staff for all public nursing manors. Currently, the Director of Community Hospitals and Continuing Care has requested that a draft business plan be completed by early March 2009.

CROWN AGENCIES - CONTROL AND ACCOUNTABILITY

10.14 Following are the outstanding recommendations resulting from our examination of Crown Agencies - Control and Accountability, as presented in the 2004 Annual Report of the Auditor General. The status of implementation of the recommendations is provided based on information received from management of the Provincial Treasury.

Auditor General's Recommendation	Status/Management Response
Treasury Board should develop requirements for corporate governance applicable to all Crown agencies.	Currently the Province's governance policies are contained within Section 10 of the Treasury Board Manual. Also, certain sections of the Financial Administration Act specify reporting requirements. Treasury Board, from time to time, does request special reviews on governance of certain Crown Corporations. However, we will conduct a review of the Governance policies with respect to their adequacy.
In addition to budgets by program area for school boards, the Budget Estimates should at a minimum provide supplementary information showing budgeted revenues and expenditures by school board.	We will take this issue up with the Department of Education for consideration.

PUBLIC ACCOUNTS COMMITTEE

11. PUBLIC ACCOUNTS COMMITTEE

ROLE AND MANDATE

11.1 The Standing Committee on Public Accounts is a Committee of the Legislative Assembly. It provides an important link in the accountability process. Through Committee proceedings members of the Committee, as members of the Legislative Assembly, are given the opportunity to hold the administration accountable for the use of public funds and the stewardship of public assets.

11.2 The Committee currently consists of nine members and is chaired by a member of the Official Opposition. It is charged with matters concerning the Public Accounts of the Province and the Auditor General's Annual Report. The Committee holds public meetings and requires the Auditor General and other witnesses to appear and answer questions on matters raised in the Auditor General's Annual Report as well as other issues.

PROCEEDINGS AND RESULTS

11.3 During the year the Committee met to complete the review of my 2007 Annual Report, my 2008 Annual Report and the Report on Government's Involvement with Natural Organic Food Group PEI Inc. Since the date of my last Annual Report up to March 1, 2009, I appeared before the Committee on seven occasions and assisted in their deliberations by providing further information, explanation, and clarification on a number of issues.

11.4 In its April 9, 2008 report to the Legislative Assembly, the Committee endorsed all the recommendations and observations in the 2007 Annual Report of the Auditor General. The Committee requested that the implementation of the recommendations be reviewed and their status be presented in the next Annual Report.

11.5 In its November 10, 2008 report to the Legislative Assembly, the Committee endorsed all the recommendations and observations in the 2008 Annual Report of the Auditor General. The Committee requested that the implementation of the recommendations be reviewed and their status be presented in the next Annual Report.

11.6 Through its deliberations the Committee has an important role in contributing to improved accountability and effectiveness in government operations. I look forward to continuing to work with the Committee in fulfilling its mandate.

OFFICE OF THE AUDITOR GENERAL

12. OFFICE OF THE AUDITOR GENERAL

MANDATE AND MISSION

12.1 The Audit Act provides the mandate for the Office of the Auditor General. As a servant of the Legislative Assembly, the Auditor General is independent of government. Authority is given to carry out financial statement audits of the Public Accounts as well as any agency of government or Crown controlled or owned corporation.

12.2 Under the Act, the Auditor General also has a broad mandate to conduct any audit or examination he considers necessary to determine whether any agency of government is achieving its purposes and is doing so economically and efficiently and is complying with the applicable statutory requirements.

12.3 The mission of the Office of the Auditor General is as follows:

- to conduct independent audits and examinations that provide objective information, recommendations, and assurance to the Legislative Assembly; and
- to promote best practices in government operations.

RESPONSIBILITIES AND FUNCTIONS

12.4 The Audit Act sets out the responsibilities of the Auditor General. The Auditor General is required to report annually on the results of the audits and examinations conducted by the Office. The work of the Office can be categorized into two main types of assignments: financial audits, and special audits and examinations.

12.5 The primary responsibility of the Auditor General is the audit of the Public Accounts of the Province. The Auditor General is also named in legislation as the financial auditor for a number of Crown agencies.

12.6 The mandate allows the Auditor General to conduct any examination considered necessary to determine whether any agency of government is achieving its purpose, is doing so economically and efficiently and is complying with the applicable statutory provisions.

Special examinations may include work on compliance with applicable authorities on a government-wide basis. In addition, the Act allows for special assignments or investigations at the request of the Lieutenant Governor in Council.

12.7 The Office performs an important service to the Legislative Assembly. In some cases, where government reports information about its performance, we comment on its completeness and accuracy and thus provide credibility and add value to that information. In other circumstances, we audit government programs directly and report our findings to the Legislative Assembly and the public. The reports resulting from these assessments include recommendations and advice which assist government in identifying opportunities for improvement in the management and control of public funds.

OPERATING PHILOSOPHY

Independence

12.8 The Auditor General is responsible to the Legislative Assembly, not government. The Office is positioned to offer impartial opinions and recommendations on government operations and management practices. The Audit Act establishes the legal framework for an independent audit office. The key components in building that independence include:

- the existence of a Legislative Audit Committee which reviews the Office's budget;
- the authority to carry out the audits and examinations which the Auditor General deems necessary;
- the right of access to records and information necessary to perform audit functions;
- the power to request and receive information or explanations required; and
- the requirement to report annually to the Legislative Assembly.

12.9 In addition, the independence of the Office is supported by our quality assurance policies and an office code of conduct which include, among other things, policy and guidance on ethics, impartiality, and potential conflict of interest situations.

Audit Planning

12.10 Each year an audit work plan is developed consistent with the audit priorities established by the Office and the resources available. The annual work plan includes a number of financial statement audits as well as special audits and examinations.

12.11 Special audits and examinations of government departments and Crown agencies are carried out on a cyclical basis. These audits can vary in scope from the entire organization to a specific division or program. Audits are sometimes carried out on a particular function on a government-wide basis.

12.12 Various factors are considered in establishing priorities for special audits and examinations. These include materiality of revenues/expenditures, results of previous audits, the date of the last audit, and the impact on the public. Other factors considered in planning each audit include; our audit mandate, expected resources required to complete the audit, the quality of the financial and management controls in place for the entity, complexity of the operations, and possible matters of significance that may arise from the audit.

Professional Standards

12.13 Generally accepted accounting principles for government are established through the recommendations of the Public Sector Accounting Board (PSAB) of the Canadian Institute of Chartered Accountants (CICA). These recommendations are directed at the public sector and deal with numerous accounting issues. We rely on generally accepted accounting principles for the public sector in conducting our audits as well as other guidance provided by the CICA.

12.14 Our audits are conducted in accordance with generally accepted assurance standards. These standards relate to the professional qualifications of auditors, minimum examination requirements, and reporting responsibilities. They are designed to ensure that our audits are properly planned, conducted, and reported and that audit findings are based on well substantiated evidence.

12.15 The Office is subject to a periodic practice inspection carried out by the Institute of Chartered Accountants of Prince Edward Island. This process is designed to protect the public interest by ensuring the Office meets the standards required of the profession. The most recent practice inspection was completed in May 2005.

PERSONNEL, ADMINISTRATION AND AFFILIATIONS

Organization

12.16 The Office staff complement consists of two audit directors, twelve auditors, one student auditor and two administrative staff. Two auditor positions remain vacant and are not funded. With our limited staff we strive to provide audit coverage of significant areas of government on a cyclical basis.

12.17 Under the Audit Act, the Legislative Audit Committee, a standing Committee of the Legislative Assembly, is responsible for the administration of the Office of the Auditor General. The Committee consists of the Speaker of the Legislative Assembly, who is Chairperson; the Leader of the Opposition; and the Provincial Treasurer. On an annual basis, the Committee reviews the budget estimates of the Office.

12.18 For the year ended March 31, 2009 the original budgeted expenditures for the Office amounted to $1,553,700 as follows.

	2008-09 Budget
Administration	$ 30,200
Equipment	7,300
Materials, Supplies, and Services	9,000
Professional and Contract Services	64,500
Salaries	1,397,900
Travel and Training	32,400
Contribution - CCAF	12,400
Total	$1,553,700

Professional Affiliations

12.19 As an Office, we strive to keep current in all aspects of legislative and other audit practices, as well as new developments within the profession. The Office maintains a close association with a number of professional organizations, and experience and methodology is shared with a view to contributing to the ongoing development of legislative audit practices. Some of the key affiliations include the following:

- The Canadian Council of Legislative Auditors (CCOLA) - The meetings of the Council bring together legislative auditors from the federal government and the provinces and provide an opportunity for information exchange, discussion, development, and enhancement of legislative audit practices. Members of the Office serve on various CCOLA committees.

- The Public Sector Accounting Board - The Office provides input and cooperates with the Board in its efforts to improve and harmonize public sector accounting practices across Canada. The Board conducts research and issues recommendations on public sector accounting issues.

- The Canadian Institute of Chartered Accountants and the Institute of Chartered Accountants of Prince Edward Island - The Office maintains an important professional relationship with these organizations and provides input and receives information on developments in the profession.

- The CCAF - The Office has been a member and supporter of the CCAF since its inception in 1980. CCAF is a Canadian research and education foundation dedicated to building knowledge for meaningful accountability and effective governance, management, and audit.

OBJECTIVES AND ACCOMPLISHMENTS

12.20 In accordance with its mandate, the Office has established two broad goals:

(I) To promote improved accountability for, and management of, public funds.

(II) To continuously update our knowledge and skills within our field of practice and to work to the highest standard of our profession.

In support of these goals, the Office has developed a number of objectives. The following paragraphs provide information on each of these objectives and the accomplishments during the year.

(i) To prepare an Annual Report for the Legislative Assembly, as required under the Audit Act, on the results of the audits that have been carried out.

12.21 The Annual Report provides information on significant issues and recommendations resulting from our work. We expect that the Annual Report presented each year will act as a vehicle for positive change in the management and performance of the public sector. The deliberations and discussions on the Report that occur within the Legislative Assembly and by the Standing Committee on Public

Accounts provide the impetus to bring about the improvements recommended in the Report.

12.22 The 2008 Annual Report of the Auditor General was tabled in the Legislative Assembly on April 8, 2008. The Report was referred to the Public Accounts Committee and the Auditor General appeared before the Committee to discuss the Annual Report and provide additional information and explanations to the Committee.

(ii) To express opinions on the financial statements of the Public Accounts of the Province and other Crown agencies subject to audit.

12.23 An unqualified opinion was provided on the Public Accounts for the year ended March 31, 2008. We continue to work closely with the Office of the Comptroller in improving the financial statement presentation and disclosure. In addition to the Public Accounts, we conduct a number of financial statement audits of Crown Corporations, Pension and Trust Funds, and other Agencies. This process provides assurance to the taxpayers, through the Legislative Assembly, on the fairness of information reported by government.

(iii) To perform selected special audits and examinations to determine whether departments and agencies are being managed with due regard for economy and efficiency and are in compliance with applicable statutory provisions.

12.24 The Office has a limited amount of resources to carry out its work. Many of the financial statement audits which we perform are required under legislation. The extent of special audit and examination work that we can undertake is determined by the resources available after the financial audit work has been assigned.

12.25 Our special audits and examinations provide information and assurance on the management of public resources in a number of areas. We provide advice and make recommendations to improve management controls and practices where problems are identified.

(iv) To perform other investigations as may be required from time to time.

Occasionally we are asked to investigate potential weaknesses in control or to follow up on specific observations from our report. This Annual Report includes the results of a special examination on Government's Involvement with Natural Organic Food Group PEI Inc. which was requested by the Lieutenant Governor in Council.

12.26 It has also been our practice to follow up on outstanding recommendations and provide information in our Annual Report on the status of implementation of the recommendations arising from our audits. This is part of the legislative audit function which provides important feedback to the Public Accounts Committee, and assists in its role of holding government accountable.

(v) To maintain technical competence in an evolving accounting and auditing environment.

(vi) To remain aware of and provide input to the development of public sector accounting standards.

(vii) To build leadership within the Office by providing professional development and training opportunities for staff.

12.27 Our Office maintains an affiliation with the Canadian Institute of Chartered Accountants which helps us to keep up to date on emerging accounting and auditing issues. Standards are promulgated by the Public Sector Accounting Board and the Assurance Standards Board. We regularly participate in this process by providing comments during the discussion stages of the development of government accounting standards. In addition, we maintain professional affiliations with the Canadian Council of Legislative Auditors and the CCAF. This participation allows us to share knowledge and experience as well as receive information on newly developed methodology.

12.28 Except for one student position, audit staff within the Office have professional accounting designations. We strive to provide

training and professional development opportunities to staff. Individual staff members attend various professional courses, conferences, seminars, and meetings.

12.29 For 2006 and subsequent years, the Institute of Chartered Accountants of PEI requires members to take a minimum of 20 hours of professional development per year and not less than 120 hours in a three year period.

SCHEDULES

OPERATING FUND
APPROPRIATIONS

ORDINARY	APPROPRIATION ACT 2007	SPECIAL WARRANTS	TRANSFERS	TOTAL BUDGET	APPROPRIATION ACT EXPENDITURES 2007/2008	UNDER EXPENDITURES 2007/2008
AGRICULTURE	$ 30,999,900	$ 6,180,000	$ -	$ 37,179,900	$ 35,894,677	$ 1,285,223
OFFICE OF THE ATTORNEY GENERAL	35,091,800	-	-	35,091,800	34,419,059	672,741
AUDITOR GENERAL	1,524,300	-	-	1,524,300	1,421,912	102,388
COMMUNITY, CULTURAL AFFAIRS AND LABOUR	43,299,700	4,420,000	-	47,719,700	45,585,128	2,134,572
DEVELOPMENT AND TECHNOLOGY	6,270,000	-	-	6,270,000	5,665,600	604,400
PEI BUSINESS DEVELOPMENT INC.	29,128,300	8,734,000	-	37,862,300	37,862,300	-
EMPLOYMENT DEVELOPMENT AGENCY	4,401,800	-	-	4,401,800	4,107,659	294,141
EDUCATION	247,680,400	2,069,700	1,889,500	251,639,600	251,034,241	605,359
ISLAND REGULATORY AND APPEALS COMMISSION	1,200,000	-	-	1,200,000	1,200,000	-
ENVIRONMENT, ENERGY AND FORESTRY	17,857,400	548,500	-	18,405,900	18,163,087	242,813
PEI ENERGY CORPORATION	597,600	-	-	597,600	486,300	111,300
EXECUTIVE COUNCIL	3,791,100	-	-	3,791,100	3,598,956	192,144
FISHERIES AND AQUACULTURE	3,645,900	50,000	-	3,695,900	3,498,160	197,740
HEALTH	376,826,200	886,300	5,693,000	383,405,500	378,235,311	5,170,189
LEGISLATIVE ASSEMBLY	5,359,100	-	-	5,359,100	4,903,003	456,097
PROVINCIAL TREASURY	33,907,800	-	-	33,907,800	30,639,484	3,268,316
GENERAL GOVERNMENT	23,439,000	-	(7,582,500)	15,856,500	13,989,150	1,867,350
EMPLOYEE BENEFITS	32,801,400	-	-	32,801,400	18,459,454	14,341,946
TECHNOLOGY ASSET MANAGEMENT	2,300,000	-	-	2,300,000	2,136,327	163,673
PEI LENDING AGENCY	5,386,500	-	-	5,386,500	5,386,500	-
COUNCIL OF ATLANTIC PREMIERS	123,500	-	-	123,500	123,500	-

Note: Appropriations and expenditures are presented in accordance with the classifications in the Appropriation Act 2007. This differs from the format used in the Operating Fund financial statements, in that amortization of tangible capital assets are recorded as expenses and tangible capital assets are capitalized in the Operating Fund financial statements.

OPERATING FUND APPROPRIATIONS

ORDINARY	APPROPRIATION ACT 2007	SPECIAL WARRANTS	TRANSFERS	TOTAL BUDGET	APPROPRIATION ACT EXPENDITURES 2007/2008	UNDER EXPENDITURES 2007/2008
PEI PUBLIC SERVICE COMMISSION	$ 5,228,600	$ 4,000	$ -	$ 5,232,600	$ 5,232,575	$ 25
SOCIAL SERVICES AND SENIORS	118,958,900	1,026,000	-	119,984,900	114,945,584	5,039,316
TOURISM PEI	22,743,300	4,051,400	-	26,794,700	22,071,492	4,723,208
INTERMINISTERIAL WOMEN'S SECRETARIAT	427,000	-	-	427,000	413,924	13,076
TRANSPORTATION AND PUBLIC WORKS	88,108,700	1,256,300	-	89,365,000	87,917,145	1,447,855
INTEREST CHARGES ON DEBT	121,201,700	-	-	121,201,700	115,883,050	5,318,650
TOTAL ORDINARY	**$1,262,299,900**	**$29,226,200**	$ -	**$1,291,526,100**	**$1,243,273,578**	**$48,252,522**
CAPITAL						
AGRICULTURE, FISHERIES AND AQUACULTURE	150,000	-	-	150,000	149,922	78
OFFICE OF THE ATTORNEY GENERAL	175,000	-	-	175,000	164,567	10,433
COMMUNITY AND CULTURAL AFFAIRS	115,000	-	-	115,000	113,301	1,699
EDUCATION	13,051,600	-	-	13,051,600	5,125,944	7,925,656
ENVIRONMENT, ENERGY AND FORESTRY	725,000	-	-	725,000	598,697	126,303
HEALTH	12,833,000	327,000	-	13,160,000	13,159,974	26
PROVINCIAL TREASURY	2,755,000	3,172,000	-	5,927,000	5,882,124	44,876
PEI PUBLIC SERVICE COMMISSION	714,400	501,400	-	1,215,800	1,172,862	42,938
SOCIAL SERVICES AND SENIORS	667,000	-	-	667,000	628,900	38,100
TOURISM PEI	1,037,500	350,000	-	1,387,500	1,347,458	40,042
TRANSPORTATION AND PUBLIC WORKS	36,636,000	7,366,600	-	44,002,600	44,002,552	48
TOTAL CAPITAL	**$ 68,859,500**	**$11,717,000**	$ -	**$ 80,576,500**	**$ 72,346,301**	**$ 8,230,199**
GRAND TOTAL	**$1,331,159,400**	**$40,943,200**	$ -	**$1,372,102,600**	**$1,315,619,879**	**$56,482,721**

Note: Appropriations and expenditures are presented in accordance with the classifications in the Appropriation Act 2007. This differs from the format used in the Operating Fund financial statements, in that amortization of tangible capital assets are recorded as expenses and tangible capital assets are capitalized in the Operating Fund financial statements.

ORDER-IN-COUNCIL	LIST OF SPECIAL WARRANTS		
	AGRICULTURE		
EC 2008-177	DIVISION MANAGEMENT		
	Grants		$4,680,000
	To provide financial support for the Atlantic Beef Products plant and beef producers.		
EC 2008-192	DIVISION MANAGEMENT		
	Grants		1, 500,000
	To provide financial support for the Atlantic Beef Products plant.		
	Total		$6,180,000
	COMMUNITY, CULTURAL AFFAIRS AND LABOUR		
EC 2008-438	MUNICIPAL AFFAIRS		
	Grants - Municipal Grants		$4,420,000
	To provide funding for municipal grants which are fully offset by real property tax revenue.		
	PEI BUSINESS DEVELOPMENT INC		
EC 2008-180	PROGRAMS		
	Grants - Infrastructure	$1,200,000	
	ASSET MANAGEMENT		
	Grants - Property Operations	570,000	$1,770,000
	To fund over expenditures identified in the 2007-08 Third Quarter Forecast. Partially offset by sequestration of funds from the general government for $1,200,000.		
EC 2008-189	PROGRAMS		
	Grants - Innovation Development Tax Credit		1,500,000
	To provide additional funding for the P.E.I. Labour Rebate Program.		

ORDER-IN-COUNCIL	LIST OF SPECIAL WARRANTS		
EC 2008-437	PROGRAMS		
	Grants - Economic Development Assistance		500,000
	To provide additional grant funding for economic development.		
EC2008-661	CORPORATE SERVICES		
	Debt - Provision for Credit Losses and Guarantee Payments		$4,964,000
	To increase the provision for credit losses and guarantee payments.		
	Total		$8,734,000
	EDUCATION		
EC 2008-178	POST SECONDARY GRANTS		
	Grants - Maritime Province's Higher Education Commission		$2,069,700
	Contribution to UPEI.		
	ENVIRONMENT, ENERGY AND FORESTRY		
EC 2008-155	RESOURCE INVENTORY AND MODELING		
	Professional and Contract Services		$ 548,500
	To fund expenditures related to acquiring LiDAR data for PEI. Fully offset by federal revenue from the Canada-Prince Edward Island National Water Program.		
	FISHERIES AND AQUACULTURE		
EC 2007-682	MARINE FISHERIES		
	Professional and Contract Services	$ 40,000	
	Travel and Training	10,000	$ 50,000
	To allow for the continuation of the Oceans and Coastal Strategy policy development. Fully offset by revenue from the federal government under the terms of Canada's Oceans Action Plan.		

ORDER-IN-COUNCIL	LIST OF SPECIAL WARRANTS		
	HEALTH		
EC 2008-140	QUEEN ELIZABETH HOSPITAL		
	Salaries	$ 125,000	
	Professional and Contract Services	36,000	
	Materials, Supplies and Services	14,000	
	Equipment	211,300	$ 386,300
	To provide additional funding for the pilot project - Provincial Strategy for Ensuring Radiation Therapy Wait Time Guarantees. Fully offset by revenue from the federal government under the terms of the Health Care Strategies and Policy Contribution Program.		
EC 2008-179	QUEEN ELIZABETH HOSPITAL		
	Materials, Supplies and Services		$ 500,000
	To fund additional drug expenditures at the PEI Cancer Treatment Center. Fully offset by sequestration of funds in Social Services and Seniors where the funds were originally budgeted.		
	Total		$ 886,300
	PEI PUBLIC SERVICE COMMISSION		
EC 2009-118	STAFFING AND HUMAN RESOURCES PLANNING		
	Salaries		$ 4,000
	To fund overexpenditures for additional staff resource to provide staffing services.		
	SOCIAL SERVICES AND SENIORS		
EC 2008-182	SOCIAL PROGRAMS		
	Materials, Supplies and Services		$1,026,000
	To fund additional renovations for various senior's housing properties across PEI. Fully offset by revenue from Canada Mortgage and Housing Corporation.		

ORDER-IN-COUNCIL	LIST OF SPECIAL WARRANTS		
	TOURISM PEI		
EC 2008-77	CORPORATE MANAGEMENT		
	Grants - Tourism PEI Inc.		$3,516,600
	To fund the accumulated losses of Golf Links PEI Inc. as of March 31, 2007.		
EC 2008-126	MARKETING		
	Administration	$ 84,700	
	Professional and Contract Services	82,500	
	TOURISM ADVISORY COUNCIL		
	Grants - Development Assistance	205,000	
	PROVINCIAL PARKS		
	Salaries	44,700	
	CORPORATE MANAGEMENT		
	Salaries	66,000	
	ADMINISTRATION		
	Grants - tourism Product Development	14,900	$ 497,800
	To fund the expenditures identified in the 2007-08 Third Quarter Forecast. Partially offset by increased revenues from Golf Links PEI of $202,800.		
EC 2008-190	TOURISM DEVELOPMENT		
	Grants - Tourism Product Development		$ 37,000
	To fund an increase in French Language Services. Fully offset by revenue under the Canada/PEI Agreement on the Promotion of Official Languages.		
	Total		$4,051,400

ORDER-IN-COUNCIL	LIST OF SPECIAL WARRANTS	
	TRANSPORTATION AND PUBLIC WORKS	
EC 2007-683	PROVINCIAL WASTE MANAGEMENT	
	Professional and Contract Services	$1,256,300
	To provide funding for cumulative operating losses of Island Waste Management Corporation incurred to March 31, 2007.	
	HEALTH - CAPITAL	
EC 2009-117	CAPITAL PROJECTS	
	Capital - Computer Equipment	$ 327,000
	To fund Clinical Information System expenditures which were reclassified from operating to capital, resulting in capital expenditures being greater than budget.	
	PROVINCIAL TREASURY - CAPITAL	
EC 2007-747	CAPITAL PROJECTS	
	Capital - Computer Equipment	$1,384,000
	To fund Connect PEI Network Project	
EC 2008-191	CAPITAL PROJECTS	
	Capital - Computer Equipment	$1,788,000
	To fund Connect PEI Network Project and procure the equipment necessary to activate the network.	
	Total	$3,172,000
	PUBLIC SERVICE COMMISSION - CAPITAL	
EC 2008-181	SYSTEMS AND ADMINISTRATION	
	Capital - Professional Services	$ 501,400
	To fund capital expenditures related to the Corporate Human Resource Management System/Payroll initiative.	

ORDER-IN-COUNCIL	LIST OF SPECIAL WARRANTS	
	TOURISM PEI - CAPITAL	
EC 2008-78	CAPITAL PURCHASES	
	Capital - Machinery and equipment	$ 350,000
	To fund capital expenditures by Golf Links PEI Inc. for fiscal 2007-08.	
	TRANSPORTATION AND PUBLIC WORKS - CAPITAL	
EC 2008-127	LAND PURCHASES	
	Capital - Land	$ 414,000
	To fund the purchase of properties. Fully offset by the sequestration of funds from the operating budget.	
EC 2008-151	LAND PURCHASES	
	Capital - Land and Building	4,340,000
	To fund the purchase of the Summerside Access P.E.I. building.	
EC 2009-119	BRIDGES	
	Capital - Development Costs	$2,612,600
	To fund additional expenditures on the Montague bridge.	
	Total	$7,366,600